2006

# Bow Valley Energy Ltd.

a clear and deliberate strategy

Bow Valley Energy Ltd.

# Bow Valley Energy has a clear and deliberate strategy to become an international, intermediate-sized exploration and production company. By leveraging off the experience and knowledge of our people, we identify and exploit niche opportunities. Our exploration and development projects are focused on proven oil basins with existing facilities and infrastructure. And we are always looking for new and innovative ways to apply technology to our operations with a view to generating strong returns for our shareholders.

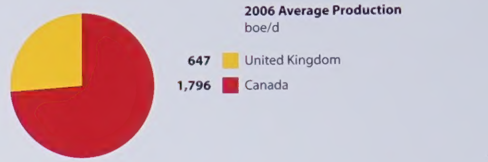
## Strategic Objectives

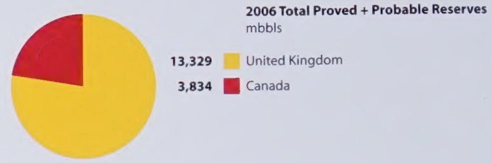
- Extend geographic diversity
- Continue development of existing properties in the U.K.
- Re-invest cash flow into U.K. exploration
- Become an operator in the North Sea
- Participate with Joint Venture partners in Alaska North Slope exploration
- Continue to pursue asset acquisition opportunities

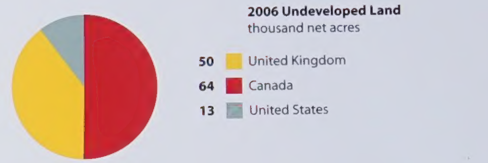
## 2006 Highlights

- Bow Valley entered into a Joint Venture Agreement with Alaska Venture Capital Group, LLC to participate in an exploration program on the North Slope of Alaska
- Closed a US$150 million debt facility with Bank of Scotland which will fund the full development of all of the Company's development assets in the U.K.
- Bow Valley participated in the drilling of two development wells at Blane, one development well at Enoch and one development well at Chestnut; results for these wells were at or above expectations
- U.K. operating costs decreased 72% year-over-year to average $7.41 per boe resulting in field operating netbacks of $58.67 per boe
- Sales volumes averaged 2,443 boe/d
- Funds flow was $20.4 million ($0.29 per share)

Geographic Contribution to Production, Reserves, Landholdings, Capital Program



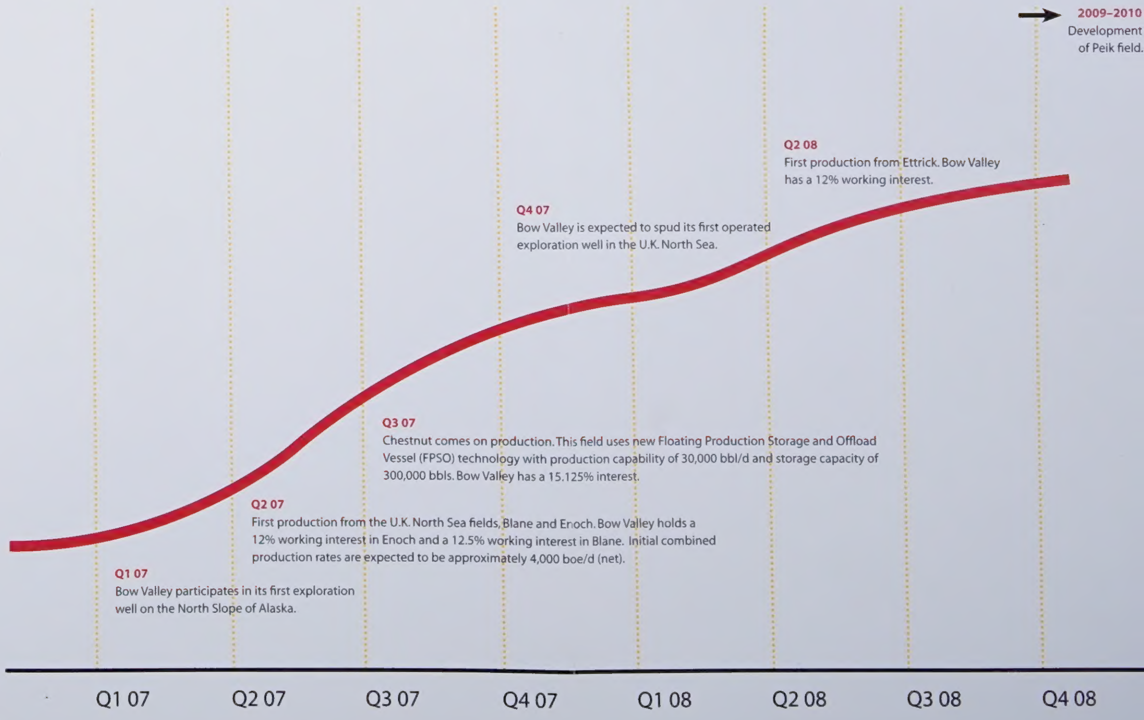


## Production Potential

This graph represents the production growth expected as new fields currently under development come on production over the next couple of years. These production additions do not include any exploration success or potential additions from the Peik field expected in the 2009–2010 time frame.

Bow Valley has tremendous exploration upside which has not been factored into this production profile. In 2005, we acquired a 70% working interest and operatorship in block 16/27a North (subsequently increased to 100% in 2007) and a 100% working interest in blocks 16/27c and 9/28b in the U.K. North Sea. Another U.K. exploration block, 22/11b, was added at a 100% working interest in 2007. Additionally, as part of a Joint Venture, we are active in the North Slope of Alaska with several exploration wells planned for 2007.

## Key Milestones





**Corporate Office**
Bow Valley Energy Ltd.
1200, 333 Seventh Avenue SW
Calgary, Alberta, Canada T2P 2Z1
Telephone: 403 232 0292
Fasimile: 403 232 8920
E-mail: bve@bvenergy.com
Website: www.bvenergy.com

**United Kingdom Office**
Bow Valley Petroleum (UK) Limited
2 Thames Avenue
Windsor, Berkshire, England SL4 1QP
Telephone: +44 (0) 1753 753 800
Facsimile: +44 (0) 1753 753 809

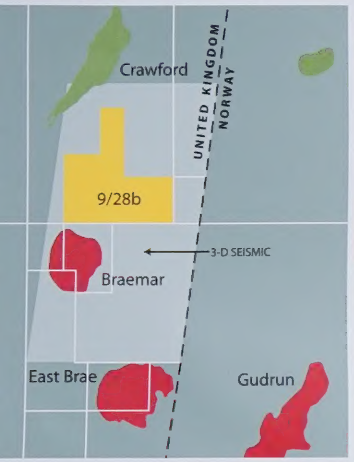

TSX: BVX

Bow Valley Energy Ltd.

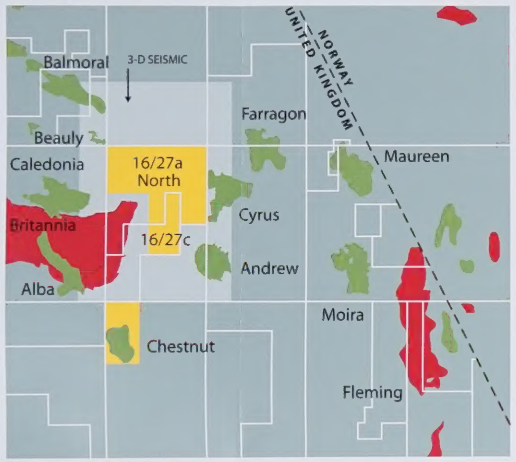
# International Operations

Bow Valley has operations in the U.K. North Sea, western Canada and the North Slope in Alaska. We regularly evaluate our assets and are continually looking for areas that will generate the best long-term value for our stakeholders. We continue to pursue exploration opportunities in conjunction with development of existing properties and asset acquisitions that support our objective to become an intermediate-sized, international exploration and production company.

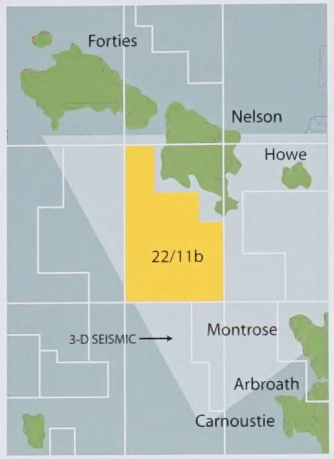
### U.K. Exploration Block – 9/28




### U.K. Exploration Block – 16/27




### U.K. Exploration Block – 22/11




Significant Gas Discovery · Significant Oil Discovery · Bow Valley Landholdings · 3-D Seismic


Joint Venture Landholdings

Oil Discoveries

Prospects/Areas

## United States

Bow Valley is participating in a joint venture to explore the North Slope of Alaska beginning in 2007.

We believe there is considerable opportunity in the North Slope. We plan to build an exploration portfolio along a proven oil fairway offsetting multi-billion barrel oil discoveries. Our exploration will target prospects that are material to Bow Valley and which can be quickly brought on stream due to existing, nearby infrastructure.

Significant discoveries in the area include:
Prudhoe Bay – 18 billion boe
Kuparuk – 3 billion boe
Endicott – 500 million boe
Alpine – 500 million boe
Milne Point – 400 million boe
Northstar – 200 million boe

Longer term, there are many other areas of Alaska that fit our investment criteria and which could lead to significant future growth.

**Discoveries 2003-2006 - New Players**

**A** Nikaitchuq discovered in 2004 contains 200 mmbo and is expected to produce 60,000 bopd

**B** Oooguruk discovered in 2003 contains 70 mmbo and is expected to come onstream in 2008 at 20,000 bopd

**C** Qanniq discovered in 2006 tested at 1,200 bopd and is expected to come on stream in 2008


## United Kingdom

Bow Valley is on course with its development of existing properties in the North Sea: Blane, Enoch, Chestnut, Ettrick and J1. At the same time we continue to evaluate additional development opportunities as evidenced by our recently announced acquisition of an interest in the Peik field. We have plans to expand our exploration efforts into other North Sea jurisdictions such as Norway.

We intend to self-finance exploration and development opportunities in the U.K. Bow Valley is placing increasing emphasis on identifying exploration prospects and will continue to acquire land through purchase, farm-ins and bid rounds. We intend to become an operator in the North Sea. In 2006, we opened our U.K. office and will continue to hire technical staff and increase our presence in the area.

BVE Producing Field

Fields to be Developed

Exploration Block

International Boundary


## Western Canada

Western Canada has been a fundamental building block for Bow Valley. In an effort to manage capital and investment risk, we have pursued a strategy of exploration, targeting moderate risk, multi-zone prospects in central Alberta and the Peace River Arch.

As part of our active management of the Company and its assets, we concluded in early 2007 that greater investment potential is available internationally. We therefore announced in February 2007 that we would seek strategic alternatives for our Canadian assets. The role of our portfolio of western Canadian properties will be reviewed as this process continues.

High Impact

Moderate Impact

# Corporate Profile

Bow Valley Energy Ltd. is an intermediate-sized, international energy company that operates in the U.K. North Sea, the North Slope of Alaska and western Canada. We are engaged in full-cycle exploration and production, including: land purchase; seismic acquisition and interpretation; drilling; facilities and pipeline construction; and the production of oil and natural gas. Our strategy balances higher-risk exploration with lower-risk development and the acquisition of producing properties. We are committed to pursuing this strategy while maintaining a strong financial position.

Bow Valley's common shares trade on the Toronto Stock Exchange under the symbol BVX.

**Notice of Meeting**

Bow Valley Energy Ltd. is pleased to invite shareholders and other interested parties to attend our Annual General and Special Meeting to be held at the Metropolitan Centre, 333 Fourth Avenue SW, Calgary, Alberta, Canada on Wednesday, May 16, 2007, commencing at 10:00 a.m. For those shareholders unable to attend the meeting, please complete and return your Form of Proxy.

**Table of Contents**

| $000s except per share amounts | 2006 | 2005 | % change |
|---|---|---|---|
| **FINANCIAL** | | | |
| Revenue | **46,512** | 62,940 | (26) |
| Funds flow | **20,377** | 31,117 | (35) |
| Basic per share ($/share) | **0.29** | 0.47 | (38) |
| Diluted per share ($/share) | **0.28** | 0.46 | (39) |
| Earnings (loss) | **(2,520)** | 6,478 | 139 |
| Basic per share ($/share) | **(0.04)** | 0.10 | 140 |
| Working capital (deficit) | **(91,397)** | (4,759) | 1,821 |
| Shares (000s) | | | |
| Basic | **72,772** | 69,225 | 5 |
| Outstanding options and warrants | **5,454** | 5,034 | 8 |
| Weighted average – basic | **69,700** | 65,693 | 6 |
| – diluted | **72,278** | 67,589 | 7 |
| **OPERATIONAL** | | | |
| **Daily Production** | | | |
| Crude oil and NGL (bbl/d) | **918** | 1,091 | (16) |
| Natural gas (mmcf/d) | **9.2** | 12.8 | (28) |
| Oil equivalent (boe/d) | **2,443** | 3,227 | (24) |
| **Prices** | | | |
| Crude oil and NGL ($/bbl) | **68.15** | 60.25 | 13 |
| Natural gas ($/mcf) | **7.09** | 8.34 | (15) |
| Oil equivalent ($/boe) | **52.15** | 53.49 | (3) |
| **Reserves** | | | |
| Proved | | | |
| Crude oil and NGL (mbbls) | **4,797** | 3,741 | 28 |
| Natural gas (bcf) | **15.9** | 19.2 | (17) |
| Oil equivalent (mbbls) | **7,444** | 6,937 | 7 |
| Proved and Probable | | | |
| Crude oil and NGL (mbbls) | **11,529** | 10,985 | 5 |
| Natural gas (bcf) | **33.8** | 37.2 | (9) |
| Oil equivalent (mbbls) | **17,162** | 17,178 | – |
| **Undeveloped land** (net acres) | | | |
| U.K. | **49,706** | 79,138 | (37) |
| Canada | **63,782** | 59,552 | 7 |
| United States | **7,845** | – | NA |

# Letter to Shareholders

**IN PAST YEARS,** Bow Valley's annual report has defined and articulated our business strategy with themes such as "Next Generation Oil", "A Dual Platform for Growth", "Clear Road Ahead" and "Gaining Momentum". In each of these years, our strategy has been clear and deliberate: to build an international, intermediate-sized, oil and natural gas company. Consistent with this plan, we have focused on developing larger reserve based pools with a medium reserve life index and modest decline rates. Our efforts have increasingly focused on the U.K. North Sea and more recently the North Slope of Alaska in the United States.

In each of these basins, there is a legacy of infrastructure. Our opportunity is to identify assets, exploration or development projects that are below the threshold of the majors but in close proximity to their infrastructure. An emerging company such as Bow Valley can capture exponential growth on satellite fields near large discoveries.

Bow Valley had an excellent year in the U.K. during 2006. Development drilling resulted in positive reserve revisions to each of our U.K. properties. Three field developments in the North Sea are expected to come on stream in the next three to six months. The development of these projects, combined with increased commodity prices, has increased the estimated net present value of our U.K. reserves by 60%.

Subsequent to year-end, Bow Valley announced the acquisition of a 66.67% interest in U.K. block 9/15a which contains a portion of the Peik field. This acquisition represents a continuation of the business strategy on which we have been so successful: developing discovered but not yet developed fields. The Peik field will represent Bow Valley's sixth field development in the U.K. The acquisition of Peik will almost double our U.K. total proved plus probable reserves. Anticipated production start-up in 2009 – 2010 should provide Bow Valley with a continued visible, growing production profile though the next three years.

We continually monitor world trends with the intent of expanding our international operations into new jurisdictions which offer a diversified asset base and significant growth potential in a stable and secure fiscal environment. As part of this effort, late in 2006, we identified an exciting opportunity on the North Slope of Alaska. Together with our co-venturers, we are participating in a multi-year, multi-well exploration program that targets prospects in close proximity to the giant Prudhoe Bay oil field. Our joint venture controls in excess of 307,000 gross acres of mineral rights and has a broad portfolio of exploration prospects that will support a multi-well drilling program over several years.

Conversely, a high cost environment and the intensely competitive nature of the Western Canadian Sedimentary Basin continue to negatively affect results from our Canadian operations. We completed a strategic review of all our assets in early 2007 and concluded that the best investment opportunities are outside of our Canadian operations. Consequently, we

made the difficult decision to seek strategic alternatives for our Canadian asset base. The role of our portfolio of western Canadian properties will be reviewed as this process continues.

Overall, we remain committed to and optimistic about our ongoing strategy of developing our U.K. properties and re-investing cash flow into an expanding exploration program in both the U.K. offshore and on the North Slope of Alaska. I am extremely pleased with the Company's progress and our emergence as a full-cycle, international, oil and natural gas company with a solid production base and an expanding exploration portfolio offering tremendous growth opportunities.

**United Kingdom**

Bow Valley enjoyed another successful and very active year in the U.K as we continued to participate in the development of four U.K. fields. At the Blane field, we participated in the drilling of two development wells, with subsea completions and began work on a tie back to the Ula production platform. First oil from this field is scheduled for the second quarter of 2007 with forecast production of approximately 18,000 (2,250 net) boe/d.

At Enoch, we participated in drilling one development well, with subsea completion and began work on a tie back to the Brae "A" production platform. First oil from Enoch is also scheduled for the second quarter of 2007 at approximately 15,000 (1,800 net) boe/d.

At Chestnut, Bow Valley participated in drilling one development well. Construction of the Sevan SSP offshore production floating facility is progressing with delivery anticipated late in the third quarter of 2007. First oil production of approximately 10,000 (1,500 net) boe/d should occur shortly thereafter. The Sevan SSP facility will be leased for 30 months with an option to extend the contract by six-month intervals.

In July 2006, Bow Valley and our partners obtained approval from the U.K. government to develop the Ettrick field and immediately entered into a contract for the construction of a floating, production, storage and offloading (FPSO) vessel using the "Aoka Mizo" hull. Fabrication is underway at shipyards in Singapore with delivery expected in early 2008. The partnership agreed to a five-year lease with an option to extend the lease if required. Drilling of three development wells is scheduled to commence in early 2007 with first oil production of approximately 20,000 (2,400 net) boe/d following delivery of the Aoka Mizo FPSO in the second quarter 2008.

A challenge to participating in these field development projects is the financing of significant capital expenditures in advance of production revenue. Bow Valley has a good relationship with Bank of Scotland, which provided project financing of US$150 million in 2006. The expanded credit is comprised of a US$125 million senior and a US$25 million mezzanine facility. Combined with the re-investment of cash flow, these credit facilities should provide

adequate funds to finance all of Bow Valley's forecasted capital commitments on each of the Blane, Enoch, Chestnut and Ettrick field developments through to their completion.

In order to finance the capital required for the Peik acquisition, we agreed to a credit-approved term sheet with Bank of Scotland for a portion of the purchase price and entered into a bought deal financing agreement with a syndicate of underwriters, led by BMO Capital Markets, for the remainder. The development capital for the field is expected to be funded out of a growing cash flow base.

We continue to assemble an inventory of exploration prospects in the North Sea in anticipation of an active drilling program beginning in 2007. Bow Valley intends to finance our exploration activities from internally generated cash flow which should dramatically increase with the advent of production from the development projects. In support of the exploration effort, Bow Valley opened an office in Windsor, U.K., and we are currently assembling a geo-technical team. During the year, we announced the appointment of Nick Fairbrother as Managing Director of our U .K. operations. Nick brings a wealth of knowledge and experience to Bow Valley and will be an integral part of our corporate plans to become an operator and active explorer in the U.K.

Bow Valley has contracted a semi submersible drilling rig for October 2007 which we intend to use for our first operated exploration well on the Navy prospect in block 16/27a North. Other exploration activity includes participating in drilling the Blackbird prospect (Bow Valley 12% working-interest) to the south of the Ettrick field in the fourth quarter of 2007. During 2006, Bow Valley also acquired approximately 700 square-kilometres of 3-D seismic data over block 9/28b (Bow Valley 100% working-interest) and we anticipate drilling this prospect in the first half of 2008. The results of the 24th offshore licensing round were announced by the U.K. government in early 2007. Bow Valley was successful in being awarded a new exploration block – 22/11b (100% working-interest). We have evaluated 3-D seismic over block 22/11b and identified two exploration prospects. As Bow Valley continues to grow, we will become more active in pursuing an exploration agenda to replace and add production and reserves.

**North Slope of Alaska**

During 2006, Bow Valley committed to participate in a multi-year, multi-well exploration program on the North Slope of Alaska. The situation is very similar to that in the U.K., where the large, multi-national oil companies discovered the easy to find giant oilfields, subsequently developed these fields with production facilities and infrastructure, but then lost interest in pursuing the remaining smaller satellite pools. The North Slope of Alaska is host to some of the largest conventional oilfields in North America, including fields such as Prudhoe Bay (13 billion bbls oil) and Kuparuk (3 billion bbls oil). It is an oil prone region with known reservoir and trapping mechanisms. In addition, the more elusive stratigraphic play concept has not

been fully explored in the area. Our Alaska partnership group is led by a team of oil patch veterans who have successfully worked the North Slope for years. This group has identified a promising portfolio of exploration prospects for which we hold great expectations.

To finance Bow Valley's initial participation in this joint venture, we completed a $17.0 million equity financing in December 2006. These funds will finance the drilling of exploration wells and the acquisition of new 3-D seismic in the 2007 winter season.

**Canada**

The past year was challenging for our Canadian operations as field activity was marred by several events. We were unable to complete our 2006 winter program in Snowfall, which resulted in the shut-in of about 400 boe/d until this 2007 winter season. A very tight market for equipment and services contributed to increased costs and delayed timing. A couple of high profile properties, including Hamelin Creek (480 boe/d) watered out, resulting in declining production volumes and significant negative reserve revisions at year-end. Despite the best efforts of our exploration team, we were unable to offset these setbacks.

Our exploration strategy for Canada has always focused on finding steady, reliable, low-risk natural gas reserves. Consistent with this strategy, we built a portfolio of low-risk, tight gas prospects. The combination of an escalating cost structure in western Canada and flat to declining natural gas prices reduced the economics of this program to marginal returns. The Western Canadian Sedimentary Basin has become extremely competitive, with the size of new discoveries declining in both reserves and deliverability. The trend of escalating finding and development (F&D) costs, higher operating costs and increased competitiveness is resulting in a major re-structuring of the industry.

When compared to Bow Valley's international portfolio, it is apparent that better investment alternatives are available outside of our Canadian operations. Accordingly, management made the difficult decision to seek strategic alternatives for our western Canadian assets. The Company has engaged Tristone Capital to assist in managing a data room process in which we will evaluate a potential re-structuring of our Canadian assets.

**Corporate Governance**

The public markets have continued to demand more stringent controls, procedures and reporting standards from reporting issuers. Bow Valley has taken on this challenge by striving to be a leader and exceeding expectations. During the year, we continued to emphasize and update our corporate governance policies and procedures. We better identified and defined risks of our business and renewed and improved the documention of the design of our control systems and reporting procedures to safeguard the integrity of our operations and the reporting thereof.

## Outlook

Bow Valley is quickly evolving into a full-cycle exploration company with a strong and diversified production base. Our strategy is to build a broad international exploration portfolio that will be largely financed using internally generated cash flow. The decision to rationalize our Canadian assets is consistent with our goal of directing capital to areas that provide the most growth with the best economic return. Bow Valley enjoys a good relationship with several financial institutions and we are confident that we can capitalize on opportunities as they present themselves.

Looking ahead to the next two years, we are extremely optimistic. Bow Valley's production, revenue and cash flow growth is forecast to be significant. We are well positioned to enjoy exploration success from a broad and diversified prospect inventory. In the U.K., the Company is making a bold move by becoming an operator of exploration and, with success, will subsequently become an operator of development and production. The move into the North Slope of Alaska is an example of our ability to recognize opportunity outside of our established areas. Overall, we believe Bow Valley will emerge as a well balanced, diversified, international oil and natural gas company.

## Acknowledgements

Bow Valley's accomplishments continue to be the result of the hard work and dedication of our employees, consultants, management and directors. Our vision to build an international, intermediate-sized oil and natural gas company is a shared goal, and our success is contingent on a committed collective effort. We thank all team members for their contribution to Bow Valley's many accomplishments. We look forward to reaching more milestones and sharing even greater success in the future.

Robert G. Moffat
*President and Chief Executive Officer*

Daryl K. Seaman
*Chairman*

March 15, 2007

Bow Valley's goal is to implement and maintain high standards of health, safety and environmental performance in all our operations. We operate in a manner designed to ensure the health and safety of our employees, contractors and the public, and to minimize adverse effects on the environment. We are committed to:

- providing practical health, safety and environmental policies and programs for all employees and contractors;
- maintaining emergency response procedures that allow personnel to respond promptly and effectively to emergencies;
- establishing training programs designed to ensure employees receive appropriate training relative to their job function;
- considering good safety performance in the process of selecting contractors, suppliers and other services;
- establishing monitoring procedures designed to ensure our operations are conducted in compliance with applicable laws and Company standards; and
- establishing reporting and investigation procedures for all injuries, serious incidents and environmental concerns.

Bow Valley has been an active operator in western Canada since 2002. We set targets of no lost time incidents and minimal impact to the environment, and we're proud to report that these goals were achieved during the year. Bow Valley is a member of the Canadian Association of Petroleum Producers' (CAPP) Environment, Health and Safety Stewardship initiative, and we are committed to the continuous improvement of our environment, health and safety performance. We are continuing to implement and plan initiatives to enhance our performance, including third-party rig and field-facility inspections; and safety-training assessments and upgrading programs for all field employees and contractors.

The broadening scope of our operations has necessitated a greater focus on the effect of our operations on the environment. We recognize the diversity of opinion that now exists among stakeholders, in particular those we connect with in rural areas, regarding the environmental effect of oil and natural gas activities. Bow Valley is committed to responding to stakeholder concerns. While we may not always share the same opinion as stakeholders, we recognize that positive, two-way communications and a willingness to consider project design alternatives can play an important role in providing an effective response and in reducing our effect on the environment.

Bow Valley, as with all offshore operators active in the exploration and production of oil and natural gas in the U.K. Continental Shelf, will also be party to a voluntary oil pollution compensation scheme known as the Offshore Pollution Liability Agreement (OPOL). Under OPOL, operating companies agree to accept strict liability for pollution damage and the cost of remedial measures. OPOL applies to all offshore facilities from which there is risk of a discharge of oil causing pollution damage.

**THIS MANAGEMENT'S DISCUSSION AND ANALYSIS** ("MD&A") provides details about Bow Valley Energy Ltd.'s ("Bow Valley" or the "Company") full year and fourth quarter 2006 financial results and compares them to the corresponding periods of 2005. In addition, this MD&A outlines the Company's capital program and outlook for 2007. It should be read in conjunction with the consolidated financial statements.

Certain statements included or incorporated by reference in this MD&A constitute forward-looking statements or forward-looking information under applicable securities legislation. Forward-looking statements or information typically contain statements with words such as "anticipate", "believe", "expect", "plan", "intend", "estimate", "propose", or similar words suggesting future outcomes or statements regarding an outlook. Although the Company believes that the expectations reflected in such forward-looking statements or information are reasonable, undue reliance should not be placed on forward-looking statements because the Company can give no assurance that such expectations will prove to be correct. Forward-looking statements or information are based on current expectations, estimates and projections that involve a number of risks and uncertainties which could cause actual results to differ materially from those anticipated by the Company and described in the forward-looking statements or information. The forward-looking statements or information contained in this MD&A are made as of the date hereof and the Company undertakes no obligation to update publicly or revise any forward-looking statements or information, whether as a result of new information, future events or otherwise, unless so required by applicable securities laws. The forward-looking statements or information contained in this MD&A are expressly qualified by this cautionary statement.

Where amounts are expressed on a barrel of oil equivalent (boe) basis, natural gas volumes have been converted to barrels of oil equivalent at six thousand cubic feet to one barrel of oil equivalent (6 mcf = 1 boe). This conversion ratio is the convention used in the oil and natural gas industry and is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead. The use of boe may be misleading, particularly if used in isolation.

All figures are reported in Canadian dollars, unless otherwise stated. Throughout this MD&A we use the term funds flow from operations (cash generated from operating activities before changes in non-cash working capital) which can be found in the statement of cash flows. This term does not have a standardized meaning under generally accepted accounting principles (GAAP) and may not be comparable to other companies' definition of the term. Management believes that funds flow is a useful supplementary measure that may assist investors. The effective date of this MD&A is March 5, 2007.

**Critical Accounting Policies**

A summary of significant accounting policies is presented in Note 1 to the consolidated financial statements. In accounting for oil and natural gas activities, the Company has a choice between two acceptable accounting policies, full cost or successful efforts. Bow Valley follows the full cost method.

## Critical Accounting Estimates

Preparing financial statements in accordance with GAAP requires management to make certain judgments and estimates. Changes to these judgments and estimates could have a material effect on the financial statements and financial position. The estimates of proved and probable reserves is critical to many aspects of the Company's financial statements, including net income through the calculation of depletion, the determination of the asset retirement obligation, the application of the ceiling test calculation and the test for impairment of goodwill. Management's judgment of fair value is also critical to the cost centre ceiling test, and test for impairment of goodwill. The carrying amount of property, plant and equipment, as well as the amount recorded for depletion, depreciation and accretion (DD&A) can be affected by these judgments. Actual results will vary and the variations may be significant.

## 2006 Overview

2006 was both a year of challenge and success for Bow Valley. The Company was active in the U.K. North Sea with the development of the Blane, Chestnut, and Enoch fields as well as field development approval and initial spending on the Ettrick field. In Canada, the Company was affected by production issues at two non-operated and one operated area that contributed to Canadian results not meeting Company expectations. The Company has made the decision to evaluate strategic alternatives for its Canadian assets (see Subsequent Events). Bow Valley entered into a new jurisdiction with the announcement of a joint venture agreement to explore on the North Slope of Alaska.

Bow Valley added value for shareholders as evidenced by the increase in the U.K. reserves and the increase in the value of these reserves. These increases were due to positive results from the drilling of the development wells, as well as higher commodity prices. The corporate reserves value increased 35% (proved plus probable, PV10, before tax) year-over-year to $415.4 million.

## Selected Financial Information

| | 2006 | | 2005 | | 2004 | |
|---|---|---|---|---|---|---|
| | **$000s** | **$/boe** | $000s | $/boe | $000s | $/boe |
| Net revenue [1] | **39,307** | **44.08** | 53,951 | 45.81 | 33,654 | 34.79 |
| Operating expense | **8,823** | **9.89** | 14,777 | 12.55 | 13,053 | 13.49 |
| Transportation expense | **793** | **0.89** | 910 | 0.77 | 678 | 0.70 |
| Operating income | **29,691** | **33.30** | 38,264 | 32.49 | 19,923 | 20.60 |
| Other corporate expenses | **9,216** | **10.34** | 6,191 | 5.27 | 5,168 | 5.34 |
| Current tax | **22** | **0.02** | 19 | 0.02 | 14 | 0.01 |
| Abandonment costs incurred | **76** | **0.09** | 937 | 0.80 | 211 | 0.22 |
| Funds flow from operations | **20,377** | **22.85** | 31,117 | 26.40 | 14,530 | 15.03 |
| Foreign exchange loss– unrealized | **2,303** | **2.58** | – | – | – | – |
| Stock based compensation | **1,934** | **2.17** | 992 | 0.84 | 466 | 0.49 |
| DD&A and amortization | **19,662** | **22.05** | 20,645 | 17.53 | 17,785 | 18.39 |
| Risk management– unrealized | **(14)** | **(0.02)** | 1,070 | 0.91 | 99 | 0.10 |
| Future income taxes (recovery) | **(912)** | **(1.02)** | 2,869 | 2.44 | (408) | (0.42) |
| Total non-cash expenses | **22,973** | **25.76** | 25,576 | 21.72 | 17,942 | 18.56 |
| Net income (loss) [2] | **(2,520)** | **(2.82)** | 6,478 | 5.48 | (3,201) | (3.31) |

| | 2006 | 2005 | 2004 |
|---|---|---|---|
| Net income (loss) | | | |
| Per share (basic and diluted) | **$(0.04)** | $0.10 | $(0.05) |
| Funds flow from operations | | | |
| Per share (basic) | **$0.29** | $0.47 | $0.23 |
| Per share (diluted) | **$0.28** | $0.46 | $0.23 |
| Total assets | **243,096** | 130,346 | 104,258 |
| Debt and working capital | | | |
| (deficiency) | **(91,397)** | (4,759) | (16,023) |

[1] Net revenue includes operating revenue less royalties plus interest and other income.

[2] Net income (loss) excludes the abandonment costs incurred. An expense is included in the Depletion, Depreciation and Accretion line item.

| | Net Revenues $000s | Net Income (loss) $000s | Net Income (loss) per share Basic ($) & Diluted ($) |
|---|---|---|---|
| **2006** | | | |
| **First quarter** | **10,810** | **1,141** | **0.02/0.02** |
| **Second quarter** | **9,102** | **613** | **0.01/0.01** |
| **Third quarter** | **11,540** | **1,047** | **0.02/0.01** |
| **Fourth quarter** | **7,855** | **(5,321)** | **(0.08)/(0.08)** |
| **Total** | **39,307** | **(2,520)** | **(0.04)/(0.04)** |
| 2005 | | | |
| First quarter | 14,962 | 1,290 | 0.02/0.02 |
| Second quarter | 13,011 | 1,445 | 0.02/0.02 |
| Third quarter | 12,054 | 584 | 0.01/0.01 |
| Fourth quarter | 13,925 | 3,159 | 0.05/0.05 |
| Total | 53,952 | 6,478 | 0.10/0.10 |

Bow Valley operates in different geographic regions (United Kingdom/Canada/United States) and with different major products focus (oil/natural gas). The Company generates the majority of its oil revenue from the United Kingdom and the majority of natural gas revenue from western Canada. This MD&A focuses on each region separately, then discusses the new Alaska operations, followed by a discussion of corporate expenses.

## CANADA

The following discussion applies to the Canadian operations **only**. Discussion regarding the Company's U.K. and Alaska operations can be found in other sections of this MD&A.

### Reserves

Bow Valley had its Canadian reserves independently evaluated as of December 31, 2006. The Company's proved plus probable reserves are considered the most likely case because there is an equal probability that the actual volumes eventually recovered will be higher or lower than the proved plus probable estimates. Company proved reserves are based on a 90% confidence level, meaning the actual volume recovered will meet or exceed the indicated Company proved reserves nine times out of ten.

Bow Valley's Reserves Committee has met with the Company's independent engineers and has reviewed and approved the reserves reports. We present the summary information following. The Company provides additional information in its Annual Information Form (AIF) and other annual filings available on the SEDAR website at www.sedar.com.

## Canadian Reserves Table (Forecast Pricing)

Company WI Reserves

| Total proved | Gas (mmcf) | Oil (mbbls) | NGL (mbbls) | BOE (mboe) |
|---|---|---|---|---|
| January 1, 2006 opening | 14,773 | 223 | 271 | 2,956 |
| Revisions | (2,006) | 103 | (2) | (232) |
| Economic factors | 20 | 2 | – | 6 |
| Drilling discoveries | 1,047 | – | 30 | 204 |
| Drilling extensions/infill | 911 | 76 | – | 228 |
| Acquisitions | – | – | – | – |
| Divestitures | – | – | – | – |
| Production | (3,078) | (87) | (56) | (656) |
| December 31, 2006 closing | 11,667 | 317 | 245 | 2,506 |

Company WI Reserves

| Total proved plus probable | Gas (mmcf) | Oil (mbbls) | NGL (mbbls) | BOE (mboe) |
|---|---|---|---|---|
| January 1, 2006 opening | 21,443 | 327 | 395 | 4,295 |
| Revisions | (3,333) | 74 | (25) | (506) |
| Economic factors | 34 | 4 | 1 | 10 |
| Drilling discoveries | 1,418 | – | 40 | 276 |
| Drilling extensions/infill | 1,324 | 189 | 5 | 414 |
| Acquisitions | – | – | – | – |
| Divestitures | – | – | – | – |
| Production | (3,078) | (87) | (56) | (656) |
| December 31, 2006 closing | 17,808 | 507 | 359 | 3,834 |

Note: Figures may not add due to rounding.

Total proved plus probable reserves decreased 11% year-over-year to 3.8 mmboe and total proved reserves decreased 15% to 2.5 mmboe as a result of reserves additions being more than offset by production volumes produced during the year and downward revisions to prior year bookings. Reserve revisions were due mainly to poor production performance at two non-operated properties (Hamelin Creek and Boucher), one operated property (Balsam) and only partially offset by positive revisions at the Company's Mikwan, Highvale and Snowfall properties.

**Canadian Revenue and Funds Flow Table**

| | 2006 | | 2005 | | % change | |
|---|---|---|---|---|---|---|
| | **$000s** | **$/boe** | $000s | $/boe | $000s | $/boe |
| Operating revenue | **30,534** | **46.58** | 40,474 | 54.57 | (25) | (15) |
| Interest and other income | **–** | **–** | 2 | – | (100) | – |
| Royalties | **(7,189)** | **(10.96)** | (9,335) | (12.59) | (23) | (13) |
| Net revenue | **23,345** | **35.61** | 31,141 | 41.98 | (25) | (15) |
| Operating expense | **7,073** | **10.79** | 5,494 | 7.41 | 29 | 46 |
| Transportation expense | **616** | **0.94** | 910 | 1.23 | (32) | 24 |
| Operating income | **15,656** | **23.88** | 24,737 | 33.34 | (37) | (28) |
| Cash costs | | | | | | |
| General and administrative costs | **3,071** | **4.68** | 2,568 | 3.46 | 20 | 35 |
| Interest expense | **1,028** | **1.57** | 842 | 1.14 | 22 | 38 |
| Foreign exchange loss (gain) | **–** | **–** | 1 | – | (100) | – |
| Abandonment costs incurred | **183** | **0.28** | 328 | 0.44 | (44) | (36) |
| Current income tax | **22** | **0.03** | 19 | 0.03 | 16 | – |
| Total cash costs | **4,304** | **6.56** | 3,758 | 5.07 | 15 | 29 |
| Funds flow from operations | **11,352** | **17.32** | 20,979 | 28.27 | (46) | (39) |
| Net Income (loss) | **(3,025)** | **(4.61)** | 4,074 | 5.48 | (174) | (184) |

| | Q4/06 | | Q4/05 | | % change | |
|---|---|---|---|---|---|---|
| | **$000s** | **$/boe** | $000s | $/boe | $000s | $/boe |
| Operating revenue | **6,635** | **45.36** | 14,172 | 69.22 | (53) | (34) |
| Interest and other income | **–** | **–** | – | – | – | – |
| Royalties | **(1,682)** | **(11.50)** | (3,367) | (16.45) | (50) | (30) |
| Net revenue | **4,953** | **33.86** | 10,805 | 52.77 | (54) | (36) |
| Operating expense | **2,024** | **13.84** | 1,535 | 7.50 | 32 | 85 |
| Transportation expense | **165** | **1.13** | 287 | 1.40 | (43) | (19) |
| Operating income | **2,764** | **18.89** | 8,983 | 43.87 | (69) | (57) |
| Cash costs | | | | | | |
| General and administrative costs | **760** | **5.20** | 901 | 4.40 | (16) | 18 |
| Interest expense | **397** | **2.71** | 214 | 1.04 | 86 | 161 |
| Foreign exchange loss (gain) | **–** | **–** | 1 | – | (100) | – |
| Abandonment costs incurred | **119** | **0.81** | 73 | 0.36 | 63 | 125 |
| Current income tax | **–** | **–** | – | – | – | – |
| Total cash costs | **1,276** | **8.72** | 1,189 | 5.80 | 7 | 50 |
| Funds flow from operations | **1,488** | **10.17** | 7,794 | 38.07 | (81) | (73) |
| Net Income (loss) | **(2,419)** | **(16.54)** | 2,265 | 11.06 | (207) | (249) |

Revenues are a product of production and prices. The following discussion outlines the Company's Canadian production levels and commodity prices, with comparisons to prior periods.

**Canadian Production**

| | 2006 | 2005 | % change | Q4/06 | Q4/05 | % change |
|---|---|---|---|---|---|---|
| Oil and NGL (bbls/d) | **391** | 276 | 42 | 356 | 360 | (1) |
| Natural gas (mcf/d) | **8,432** | 10,534 | (20) | 7,401 | 11,191 | (34) |
| Oil and natural gas equivalent (boe/d) | **1,796** | 2,032 | (12) | 1,590 | 2,225 | (29) |

Canadian production volumes were below expectations mainly due to the unexpected loss of production at two non-operated properties (Hamelin Creek and Boucher), and one operated area (Balsam) in the first quarter of the year. This loss of production resulted in 2006 Canadian production averaging 1,796 boe/d versus 2,032 boe/d in 2005 representing a decrease of 12%. Canadian production was down 29% in the fourth quarter of 2006 to 1,590 boe/d from 2,225 boe/d in the fourth quarter of 2005 for the reasons outlined above.

**Prices**

| | 2006 | 2005 | % change | Q4/06 | Q4/05 | % change |
|---|---|---|---|---|---|---|
| Natural gas | | | | | | |
| Aeco (Cdn$/mcf) | **6.53** | 8.73 | (25) | 6.91 | 11.37 | (39) |
| Corporate average (Cdn$/mcf) | **7.13** | 9.18 | (22) | 7.49 | 11.87 | (37) |
| Oil and NGL | | | | | | |
| WTI Cushing (US$/bbl) | **66.22** | 56.47 | 17 | 60.06 | 60.03 | – |
| Edmonton light (Cdn$/bbl) | **73.72** | 68.86 | 7 | 65.14 | 72.19 | (10) |
| Corporate average (Cdn$/bbl) | **59.65** | 50.54 | 18 | 46.15 | 57.33 | (20) |
| Total operating revenue (Cdn$/boe) | **46.58** | 54.57 | (15) | 45.36 | 69.22 | (34) |
| US$/Cdn$ exchange | **0.882** | 0.825 | 7 | 0.878 | 0.852 | 3 |

*Natural Gas*

The Company's natural gas is sold on a daily Alberta spot market price basis. Western Canadian natural gas prices are referenced to the AECO Hub in Alberta. The Company generally receives a small premium to AECO prices due to the higher heat content of its natural gas. In 2006, corporate prices averaged $7.13 per mcf, down 22% from the previous year. There were no natural gas hedges in place during 2006 or 2005. Corporate prices averaged $7.49 per mcf in the fourth quarter of 2006 ($11.87 per mcf in the fourth quarter of 2005).

*Oil and Natural Gas Liquids*

The benchmark price for oil in North America is West Texas Intermediate (WTI). Western Canadian oil prices are referenced to the posted reference price at Edmonton, Alberta, which represents the WTI price adjusted for currency, transportation and quality differentials. Bow Valley's liquids production includes pentanes plus, butane, propane and ethane and normally results in a lower price compared to the Edmonton Light crude oil reference price. In 2006, this discount averaged $14.07 per barrel.

**Royalties**

| | 2006 $000s | 2005 $000s | % change | Q4/06 $000s | Q4/05 $000s | % change |
|---|---|---|---|---|---|---|
| Crown royalties | **5,823** | 7,915 | (26) | 1,333 | 2,873 | (54) |
| Other royalties | **1,866** | 1,920 | (3) | 474 | 619 | (23) |
| | **7,689** | 9,835 | (22) | 1,807 | 3,492 | (48) |
| Alberta Royalty Tax Credit | **(500)** | (500) | – | (125) | (125) | – |
| Net royalties | **7,189** | 9,335 | (23) | 1,682 | 3,367 | (50) |
| % of operating revenue | **24%** | 24% | – | 26% | 24% | 8 |

Royalties in Canada are payable to the Crown and others on a sliding scale or fixed basis, with adjustments based on prices, well productivity and product quality. The Alberta Royalty Tax Credit (ARTC) is a credit paid by the Alberta government and is subject to a maximum. The Company reached this annual maximum in 2006. The Alberta government has cancelled the ARTC program and therefore the Company will not receive any related benefit in 2007.

The decrease in crown royalties in 2006 is due to decreased production and lower prices on both the year-over-year comparison as well as the quarter-over-quarter comparison.

**Operating Costs**

| | 2006 | 2005 | % change | Q4/06 | Q4/05 | % change |
|---|---|---|---|---|---|---|
| Operating costs ($000s) | **7,073** | 5,494 | 29 | 2,024 | 1,535 | 32 |
| Operating costs ($/boe) | **10.79** | 7.41 | 46 | 13.84 | 7.50 | 85 |

Total operating costs were higher in 2006 versus 2005 for both the year-over-year comparison and the quarter-over-quarter comparison due to cost inflation for field services in the western Canadian basin. Unit operating costs were up in 2006 due to cost inflation for field services and fixed costs being allocated over a smaller production base.

The vast majority of Bow Valley's natural gas production is gathered, processed and/or compressed through third-party facilities on a fee basis. These fees are between $0.40 and $1.00 per mcf ($2.40 – $6.00 per boe) depending upon the facilities accessed. Utilizing third-party facilities generally results in higher per unit production costs than using Company-owned facilities, but also reduces the time and capital required to bring new discoveries on stream. Using third-party facilities also allows the Company to maximize capital available for exploration and drilling activities. It also permits greater flexibility in accommodating a broad spectrum of expected production rates and project life spans that would be difficult to achieve cost effectively through Company-owned facilities.

**Depletion, Depreciation and Accretion**

| | 2006 $000s | 2005 $000s | % change | Q4/06 $000s | Q4/05 $000s | % change |
|---|---|---|---|---|---|---|
| Total depletion, depreciation and accretion | **14,483** | 13,430 | 8 | 3,970 | 3,761 | 6 |
| Total depletion, depreciation and accretion ($/boe) | **22.09** | 18.10 | 22 | 27.14 | 18.37 | 48 |

In 2006, aggregate DD&A expense was higher due to a higher DD&A rate offset by decreased production volumes. Unit DD&A expense increased due to the lower total proved reserves as discussed in the Canada Reserves section of this MD&A. Fourth quarter DD&A was higher year-over-year and on an absolute basis because of the higher per-unit cost based on the updated reserve estimates recorded in the fourth quarter of 2006.

### Goodwill

At December 31, 2006, the Company had $8.5 million in goodwill (2005 – $8.5 million) recorded on its balance sheet, arising from the Company's acquisition of Boundary Creek Resources Ltd. in 2002.

The Company recorded no additional goodwill in 2006. The Company does not amortize goodwill but tests it at least annually for impairment. The Company has made no provision for impairment of goodwill at December 31, 2006. Goodwill could become impaired in the future and in such event, a write-down would occur.

### U.K.

The following discussion applies to the Company's U.K. operations **only.** Discussion regarding the Company's Canadian and Alaska operations can be found in other sections of this MD&A.

### Reserves

Bow Valley had its U.K. reserves independently evaluated as of December 31, 2006. The Company's proved plus probable reserves are considered the most likely case because there is an equal probability that the actual volumes eventually recovered will be higher or lower than the proved plus probable estimates. Company proved reserves are based on a 90% confidence level, meaning the actual volume recovered will meet or exceed the indicated Company proved reserves 9 times out of 10.

Bow Valley's Reserves Committee has met with the Company's independent engineers and has reviewed and approved the reserves reports. We present the summary information below. The Company provides additional information in its Annual Information Form (AIF) and other annual filings available on the SEDAR website at www.SEDAR.com.

**U.K. Reserves Table (Forecast Pricing)**

Company WI Reserves

| Total proved | Gas (mmcf) | Oil (mbbls) | NGL (mbbls) | BOE (mboe) |
|---|---|---|---|---|
| January 1, 2006 opening | 4,401 | 3,247 | – | 3,980 |
| Revisions | 78 | 1,188 | – | 1,201 |
| Drilling discoveries | – | – | – | – |
| Drilling extensions/infill | – | – | – | – |
| Acquisitions | – | – | – | – |
| Divestitures | – | – | – | – |
| Production | (264) | (200) | – | (244) |
| December 31, 2006 closing | 4,215 | 4,235 | – | 4,937 |

Company WI Reserves

| Total proved plus probable | Gas (mmcf) | Oil (mbbls) | NGL (mbbls) | BOE (mboe) |
|---|---|---|---|---|
| January 1, 2006 opening | 15,711 | 10,114 | 149 | 12,882 |
| Revisions | 545 | 600 | – | 691 |
| Drilling discoveries | – | – | – | – |
| Drilling extensions/infill | – | – | – | – |
| Acquisitions | – | – | – | – |
| Divestitures | – | – | – | – |
| Production | (264) | (200) | – | (244) |
| December 31, 2006 closing | 15,992 | 10,514 | 149 | 13,329 |

Total proved reserves increased by 24% to 4.9 mmboe, due to the reclassification of reserves from the probable to the proved category at the Chestnut field and positive reserve revisions at the Blane, Enoch and Kyle fields. Proved plus probable reserves increased by 0.45 mmboe, after production of 0.24 mmboe. There were positive reserve revisions at the Kyle field due to better than expected reservoir performance and the anticipated use of gas lift. Further positive revisions at the Blane and Enoch fields followed the better than expected completion results from field development wells.

**U.K. Revenue and Funds Flow Table**

| | **2006** | | 2005 | | % change | |
|---|---|---|---|---|---|---|
| | **$000s** | **$/boe** | $000s | $/boe | $000s | $/boe |
| Operating revenue | **15,978** | **67.66** | 22,466 | 51.51 | (29) | 31 |
| Interest and other income | **106** | **0.45** | 115 | 0.27 | (8) | 67 |
| Royalties | **(302)** | **(1.28)** | (643) | (1.47) | (53) | (13) |
| Net revenue | **15,782** | **66.83** | 21,938 | 50.31 | (28) | 33 |
| Operating expense | **1,750** | **7.41** | 9,283 | 21.28 | (81) | (65) |
| Transportation expense | **177** | **0.75** | – | – | n/a | n/a |
| Operating income | **13,855** | **58.67** | 12,655 | 29.03 | 9 | 102 |
| Cash costs | | | | | | |
| General and administrative costs | **1,490** | **6.31** | 957 | 2.19 | 56 | 188 |
| Interest expense | **31** | **0.13** | 320 | 0.73 | (90) | (82) |
| Foreign exchange loss (gain) | **1,532** | **6.49** | (161) | (0.37) | (1,052) | (1,854) |
| Risk management loss (gain) | **420** | **1.78** | 928 | 2.13 | (55) | (16) |
| Abandonment costs incurred | **(107)** | **(0.45)** | 609 | 1.40 | (118) | (132) |
| Total cash costs | **3,366** | **14.26** | 2,653 | 6.08 | 27 | 135 |
| Funds flow from operations | **10,489** | **44.41** | 10,002 | 22.95 | 5 | 94 |
| Net income (loss) | **2,159** | **9.14** | 2,613 | 5.99 | (17) | 53 |

| | Q4/06 ($000s) | Q4/06 ($/boe) | Q4/05 ($000s) | Q4/05 ($/boe) | % change ($000s) | % change ($/boe) |
|---|---|---|---|---|---|---|
| Operating revenue | **3,000** | **63.07** | 2,988 | 58.01 | 0 | 9 |
| Interest and other income | **15** | **0.32** | 35 | 0.68 | (57) | (53) |
| Royalties | **(91)** | **(1.91)** | (145) | (2.81) | (37) | (32) |
| Net revenue | **2,924** | **61.48** | 2,878 | 55.88 | 2 | 10 |
| Operating expense | **268** | **5.63** | 295 | 5.73 | (9) | (2) |
| Transportation expense | **59** | **1.24** | – | – | n/a | n/a |
| Operating income | **2,597** | **54.61** | 2,583 | 50.15 | 1 | 9 |
| Cash costs | | | | | | |
| General and administrative costs | **546** | **11.48** | 249 | 4.83 | 119 | 138 |
| Interest expense | **5** | **0.11** | 115 | 2.23 | (96) | (95) |
| Foreign exchange loss (gain) | **1,476** | **31.03** | (279) | (5.42) | (629) | (673) |
| Risk management loss (gain) | **38** | **0.80** | 70 | 1.36 | (46) | (41) |
| Abandonment costs incurred | **–** | **–** | 427 | 8.29 | (100) | (100) |
| Total cash costs | **2,065** | **43.42** | 582 | 11.29 | 255 | 285 |
| Funds flow from operations | **532** | **11.19** | 2,001 | 38.86 | (73) | (71) |
| Net income (loss) | **(2,890)** | **(60.76)** | 993 | 19.27 | (391) | (415) |

Revenues are a product of production and prices. The following discussion outlines the Company's U.K. production levels and commodity prices with comparisons to prior periods.

**U.K. Sales Volumes**

| | **2006** | 2005 | % change | Q4/06 | Q4/05 | % change |
|---|---|---|---|---|---|---|
| Oil (bbls/d) | **527** | 815 | (35) | 367 | 392 | (6) |
| Natural gas (mcf/d) | **722** | 2,278 | (68) | 902 | 1,007 | (10) |
| Oil and natural gas equivalent (boe/d) | **647** | 1,195 | (46) | 517 | 560 | (8) |

The Kyle field is the Company's only producing field in the U.K. North Sea. The field produces into a floating production storage and offloading vessel ("FPSO") and the Company records sales when the inventory is offloaded (lifted) to a shuttle tanker and sold. Oil sales were lower in 2006 due to fewer liftings and lower production levels than 2005 and an increase in the amount of oil in inventory at year-end (31,000 barrels in 2006 compared to 23,000 barrels in 2005). Natural gas production is sold on a continuous basis, and revenue is recognized when produced. Natural gas production was lower year-over-year due to a temporary field shut-in for maintenance, as well as natural declines.

## Prices

| | 2006 | 2005 | % change | Q4/06 | Q4/05 | % change |
|---|---|---|---|---|---|---|
| Natural gas | | | | | | |
| Corporate average (Cdn$/mcf) | **6.33** | 4.46 | 42 | 8.66 | 5.74 | 51 |
| Oil and NGL | | | | | | |
| Brent (US$/bbl) | **65.85** | 54.72 | 20 | 60.07 | 56.98 | 5 |
| Corporate average (Cdn$/bbl) | **74.47** | 63.55 | 17 | 67.68 | 68.15 | (1) |
| Total operating revenue (Cdn$/boe) | **67.66** | 51.51 | 31 | 63.07 | 58.01 | 9 |
| US$/Cdn$ exchange | **0.882** | 0.825 | 7 | 0.878 | 0.852 | 3 |

*Oil*

The benchmark price for oil in the U.K. North Sea is Brent crude. Brent generally trades at a discount to WTI, with that discount varying due to the relative demand for oil between Europe and North America, as well as tanker costs for transporting oil between the two continents. Prices were higher for the full year and fourth quarter compared to the prior year due to stronger Brent prices and a weaker Canadian dollar. In the U.K., oil sales volumes from the Kyle field received a slight premium compared to the Brent benchmark price. In 2006, that premium averaged US$0.60 per barrel (2005 – US$0.92 per barrel). In the fourth quarter the premium averaged US$0.65 per barrel (2005 – US$2.01 per barrel).

*Natural Gas*

In the U.K., natural gas is contracted with the price recalculated on an annual basis each October. The price is set based on a formula indexed by an average of the price of several energy related products for the previous year in the U.K., as well as historical index prices for natural gas. The only price variable during the year results from fluctuations in the British pound sterling to Canadian dollar exchange rate.

## Royalties

There is no crown royalty payable on oil or natural gas production in the U.K. The Company is required to pay a gross overriding royalty of US$0.10 per barrel on oil production from the Kyle field to a third party, as well as a net profits interest (NPI) based on the results of the Kyle field. In 2006, the royalty and NPI were $0.3 million (2005 – $0.6 million).

## Operating Costs

| | 2006 | 2005 | % Change | Q4/06 | Q4/05 | % Change |
|---|---|---|---|---|---|---|
| Operating costs ($000s) | **1,750** | 9,283 | (81) | 268 | 295 | (9) |
| Operating costs ($/boe) | **7.41** | 21.29 | (65) | 5.63 | 5.73 | (2) |

Operating expenses for production from the Kyle field are largely related to processing fees for the oil, which is processed through the Ramform Banff on a tariff basis. Operating costs decreased 81% to $1.8 million for 2006 from $9.3 million in 2005. The significant decrease on both a total and a per unit basis is due to Kyle oil production being redirected from a different FPSO, which had a high fixed cost, resulting in a high per unit cost, to the Ramform Banff, which processes the oil from the Kyle field on a fixed tariff basis. The Ramform Banff has been processing Kyle oil on a fixed tariff basis exclusively since September 2005. Operating costs of

$0.1 million relating to oil produced, but not sold, have been included in other assets (2005 – $0.2 million).

**Depletion, Depreciation and Accretion**

| | 2006 | 2005 | % Change | Q4/06 | Q4/05 | % Change |
|---|---|---|---|---|---|---|
| Total depletion, depreciation and accretion ($000s) | **5,048** | 6,870 | (27) | 1,207 | 929 | 30 |
| Total depletion, depreciation and accretion ($/boe) | **21.37** | 15.76 | 36 | 25.38 | 18.04 | 41 |

U.K. total DD&A expense decreased from 2005 due to the lower sales volumes during the year. The higher per unit DD&A rate in 2006 is mainly due to an increase in the estimate of future capital associated with the total proved reserves as evaluated by GLJ, as well as an unsuccessful exploration well that was drilled in the first quarter of 2006. The fourth quarter DD&A and DD&A per unit was higher due to the increase in future capital associated with the proved reserves.

**ALASKA**

The Company entered into a joint venture agreement late in 2006, which will see the Company participate in a capital expenditure program on the North Slope in 2007. At year end, there were no oil and gas reserves attributed to the Company's interests. The Company spent $1.9 million in Alaska in 2006

**CORPORATE**

**Interest Expense**

Bow Valley recorded $1.1 million of interest expense for 2006 (2005 –$1.2 million). Interest expense for the fourth quarter for of 2006 was $0.4 million, compared to $0.3 million for 2005. In the U.K., the Company capitalized $6.8 million of interest associated with the development projects (2005 – nil).

**General and Administrative Expenses**

| | 2006 $000s | 2005 $000s | % change | Q4/06 $000s | Q4/05 $000s | % change |
|---|---|---|---|---|---|---|
| Regular G&A | **4,660** | 4,138 | 13 | 1,173 | 1,326 | (10) |
| U.K. office [1] | **1,490** | 957 | 56 | 546 | 249 | 119 |
| Stock based compensation | **1,934** | 992 | 95 | 482 | 330 | 46 |
| Lawsuit defense | **1,702** | 719 | 137 | 9 | 179 | (95) |
| Overhead recoveries | **(552)** | (586) | (6) | (122) | (161) | (24) |
| Subtotal | **9,234** | 6,220 | 48 | 2,088 | 1,923 | 9 |
| Capitalized overhead | **(995)** | (968) | 3 | (249) | (248) | 0 |
| G&A as reported | **8,239** | 5,252 | 57 | 1,839 | 1,675 | 10 |

[1] Allocated amount

General and administrative expenses (G&A) for 2006 were $8.2 million, compared to 2005 expenses of $5.3 million. The higher costs related to an increase in the costs of compliance with new securities regulations, higher cash and non-cash compensation related to a higher staff complement, initial costs related to the opening and staffing of the U.K. office and increased costs to defend a lawsuit as outlined in Note 14 to the financial statements. Fourth quarter 2006 G&A was $1.8 million, an increase of 10% from the $1.7 million in the fourth quarter of 2005.

**Foreign Exchange**

Bow Valley's wholly-owned subsidiary Bow Valley Petroleum (UK) Limited has a bank facility that is denominated in U.S. dollars and Bow Valley's wholly-owned subsidiary Bow Valley Alaska Corporation operates in U.S. dollars. U.K. production revenue is denominated in U.S. dollars, while current accounts, including accounts payable, are typically denominated in British pounds sterling. As a result of the fluctuations in the value of the Canadian dollar versus the United States dollar and British pounds sterling between the time the revenue, expenses, debt and payables were incurred and the time they were repaid or valued on the balance sheet dates, the Company incurred a total loss of $3.7 million for 2006, of which $1.4 million was realized and $2.3 million was unrealized (2005 – realized gain of $0.2 million) including a 2006 fourth quarter loss of $4.1 million, of which $1.5 million was realized and $2.6 million was unrealized (2005 – realized gain of $0.3 million).

**Asset Retirement Obligation**

At December 31, 2006, the present value of the Company's asset retirement obligation was $11.9 million (2005 – $11.0 million). The total undiscounted expected cost of abandonment and site reclamation is $18.9 million and is expected to be paid over the next 35 years with the majority between 2012 and 2019.

**Other Assets**

Current other assets include $0.8 million (2005 – $0.5 million) of oil produced but not sold at December 31, 2006, relating to U.K. operations. A cost recovery amount of $0.1 million (2005 – $0.3 million) in respect of the Company's service contract with the National Iranian Oil Company to develop the Balal oilfield has also been included in current other assets.

Non-current other assets include premiums of $0.7 million (2005 – $0.3 million) relating to U.K. put option contracts associated with the Company's risk management program.

**Taxes**

Current tax expense relates solely to Canadian capital taxes paid by Bow Valley Energy Ltd. No cash income taxes were payable in either 2006 or 2005.

The Company recorded a future tax recovery of $1.9 million related to the Canadian operations for 2006 compared to a provision of $2.8 million in 2005. The Canadian recovery in 2006 mainly relates to the reduction in Canadian tax rates enacted during the year. The Company recorded a provision of $0.9 million for 2006 related to the U.K. operations (2005 – $0.1 million). The increased provision in the U.K. mainly relates to the profitable operations at the Kyle field. During 2006, the Company recognized a $17.5 million future tax asset which reduced the cost

base of the U.K. property plant and equipment. The future tax asset recognized relates to the future benefit of eligible capital exploration expenditures in accordance with the Exploration Expenditure Supplement enacted in the U.K. The Company does not expect to pay cash income taxes for the next two years in the United Kingdom or Canada.

The Company has tax pools available of $63.3 million in Canada (2005 – $47.1 million) and $127.7 million in the U.K. (2005 – $34.3 million).

## Capital Costs

| Canada | **2006 $000s** | 2005 $000s | % change | Q4 /06 $000s | Q4 / 05 $000s | % change |
|---|---|---|---|---|---|---|
| Land and lease costs | **3,837** | 4,044 | (5) | 11 | 849 | (99) |
| Geological and geophysical | **1,300** | 1,131 | 15 | 30 | 674 | (96) |
| Drilling and completion | **18,310** | 16,179 | 13 | 2,809 | 4,869 | (42) |
| Tangible production equipment | **6,225** | 5,654 | 10 | 919 | 1,773 | (48) |
| Other | **1,149** | 1,017 | 13 | 351 | 295 | 19 |
| Total | **30,821** | 28,025 | 10 | 4,120 | 8,460 | (51) |

| U.K. | | | | | | |
|---|---|---|---|---|---|---|
| Acquisition | **1,333** | 1,395 | (4) | 1,333 | 1,228 | 9 |
| Development | **80,493** | 9,963 | 708 | 45,997 | 5,277 | 772 |
| Exploration | **6,963** | 130 | 5,257 | 1,706 | 127 | 1,243 |
| Total | **88,789** | 11,488 | 673 | 49,036 | 6,632 | 639 |

| Alaska | | | | | | |
|---|---|---|---|---|---|---|
| Land and lease costs | **1,859** | – | NA | 1,859 | – | NA |

In Canada, capital costs of $30.8 million were incurred in 2006, a 10% increase from 2005. The increase reflects the Company's expanded activities over the past year in western Canada, as well as cost pressures that are affecting the industry.

In the U.K., capital costs of $88.8 million were incurred in 2006, a 673% increase from 2005 reflecting the development of the Company's U.K. fields, as well as an unsuccessful exploration well drilled in the first quarter of 2006.

In Alaska, capital costs of $1.9 million were incurred in 2006, the costs are the Company's portion of prior costs incurred by the operator and represent the initial spending for the exploration program on the North Slope.

### Land

| (acres) | Undeveloped Gross | Undeveloped Net | Developed Gross | Developed Net |
|---|---|---|---|---|
| U.K. | 117,548 | 49,706 | 5,585 | 798 |
| Alaska | 39,226 | 7,845 | – | – |
| Canada | 98,700 | 63,782 | 67,809 | 30,540 |
| Total | 255,474 | 121,333 | 73,394 | 31,338 |

### Drilling Activity

| | U.K. Gross | U.K. Net | Canada Gross | Canada Net |
|---|---|---|---|---|
| Oil | 3 | 0.4 | – | – |
| Natural gas | – | – | 9 | 7.7 |
| Service | 1 | 0.2 | – | – |
| Abandoned | 1 | 0.1 | 3 | 1.5 |
| Suspended | – | – | 5 | 3.6 |
| Total | 5 | 0.7 | 17 | 12.8 |

### Liquidity and Capital Resources

At December 31, 2006, the Company had a working capital deficiency of $91.4 million which includes bank drawings of $76.4 million. The Company is able to finance this deficiency through bank lines and funds flow from operations. The Company has bank facilities in the U.K. with an approved limit of US$150.0 million. At December 31, 2006, US$43.7 million was drawn on this facility. In Canada, the Company had a $27.5 million facility, which was subsequently amended to $30.0 million (see Subsequent Events). At December 31, 2006, the Company had approximately $25.5 million drawn on this facility.

The Company has 73,153,117 shares outstanding and 5,073,330 options outstanding as at March 5, 2007.

### Commodity Risk Management

In conjunction with the Company's bank facilities, the Company has entered into several risk management contracts designed to improve risk-adjusted returns and to ensure adequate cash flows to repay the bank facilities. The Company's risk management policy is outlined in Note 1(h) to the Financial Statements. In 2006, the Company incurred an unrealized gain of $0.01 million and a realized loss of $0.4 million due to risk management contracts. In 2005, unrealized risk management losses were $1.1 million and realized losses were $0.9 million. In the fourth quarter of 2006, the Company had an unrealized gain of $0.3 million and a realized loss of $0.04 million. There was an unrealized loss of $0.5 million and a realized loss of $0.1 million in the fourth quarter of 2005.

### Contractual Requirements/Commitments

The Company had the following risk management commitments and contracts outstanding at December 31, 2006:

| Type | Time Frame | Volume | Price ($US) | Basis |
|---|---|---|---|---|
| Costless Collars | First Half 2007 | 181,000 (floor) | US$40.00 | Brent |
| | | 90,500 (ceiling) | US$67.50 | |
| Puts | First Half 2007 | 181,000 | US$40.00 | Brent |
| | Third Quarter 2007 | 184,000 | US$40.00 | Brent |
| | Fourth Quarter 2007 | 228,160 | US$40.00 | Brent |
| | 2008 | 366,000 | US$50.00 | Brent |

The Company is participating in four field developments in the U.K. The Company will incur an estimated $65 million in capital costs over the next two years in respect of these developments. The timing and costs are subject to change based on the ability of the operators to complete the field developments as planned. The Company expects to finance these commitments through bank lines and funds flow from operations.

The Company entered into a joint venture agreement with Alaska Venture Capital Group, LLC in the fourth quarter of 2006. The Company has committed to spend an estimated $13 million in capital costs in 2007. The Company expects to finance these commitments through the recently completed $17.0 million equity financing closed on December 11, 2006.

The Corporation has contracted a drilling rig for one North Sea offshore well expected to be drilled in the fourth quarter of 2007. The estimated financial commitment is approximately US$16.5 million.

The Company's office lease commitments and transportation commitments are outlined in Note 13.

### Controls

The Company has established disclosure controls, procedures and corporate policies so that the consolidated financial results are presented accurately, fairly and in a timely manner in all material respects. The disclosure controls and procedures are designed to provide reasonable assurance that all material information required to be disclosed in reports filed or submitted under applicable securities regulations is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. The Company's President and Chief Executive Officer and Vice President, Finance and Chief Financial Officer have evaluated the effectiveness of the Company's disclosure controls and procedures as of the end of the period covered by the Company's annual filings and have concluded, based upon their evaluation, that the disclosure controls and procedures are effective to provide reasonable assurances that all material information required to be disclosed by the Company is accumulated and communicated to management. Management recognizes that all internal control systems, no matter how well designed, have inherent limitations. Therefore, management has concluded

that these systems provide reasonable, but not absolute assurance, that financial information is accurate and complete in all material respects. Any control system, no matter how well conceived or operated, can provide only reasonable, not absolute assurance, that the objectives of the control system are met.

The Company's President and Chief Executive Officer and Vice President, Finance and Chief Financial Officer confirm there have been no changes in the Company's internal control over financial reporting that occurred during the most recent interim period that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

**Subsequent Events**

On February 20, 2007, the Company announced that it had engaged a financial advisor to assist in evaluating strategic alternatives for its Canadian assets. While it is likely that this process will lead to the disposition of all or a portion of the Canadian assets, there is no assurance that this will be the case, nor is any forecast given as to the form of action that will be taken, if any. An estimate of the financial impact, if any, of the potential disposition cannot be made at the current time.

On February 21, 2007, the Company agreed to a new bank line with the National Bank of Canada regarding its Canadian assets. The new line consists of a $22.5 million senior facility plus a $7.5 million term facility due May 31, 2007. The Company believes this new facility will be adequate to meet its near term capital and liquidity needs. The term facility is expected to be repaid through cash flow and the sale of some or all of the Canadian assets.

**Outlook/Business Risks**

In Canada, Bow Valley has significantly reduced its capital expenditure budget due to the decision to evaluate strategic alternatives for its Canadian assets. This process may lead to the disposition of some or all of its Canadian assets. At the conclusion of this process, the Company will review its Canadian capital expenditure budget, and will revise it as necessary.

In the U.K., the Company is forecasting capital spending of approximately $75 million, which is expected to cover remaining expenditures to bring the Enoch, Blane, and Chestnut fields on production, provide initial capital spending for the development of the Ettrick field and fund $20 million in exploration activities, including the drilling of two exploration wells.

In Alaska, the Company is forecasting capital spending of approximately $13 million, for the committed exploration expenditures relating to the Company's joint venture on the North Slope.

The planned spending will be funded out of funds flow from operations, $17 million of cash raised from an equity issue that closed late in 2006, and currently available bank lines. The Company continues to evaluate potential acquisition opportunities, which would likely be financed through a combination of new debt and equity.

2007 activities will emphasize more exploration activity, which carries greater risks than project developments. The Company expects this increased emphasis on exploration to continue into 2008.

The Company expects commodity prices to continue above long-term averages with high levels of volatility, reflecting tight supply and demand fundamentals. World political events, which are impossible to predict, will continue to influence both oil and natural gas prices. High commodity prices have created strong global demand for oil and natural gas services, resulting in significant cost pressures for these services. Higher costs have a negative effect on the investment returns received on the Company's projects, while reduced availability of services can lead to project delays.

The Company's financial and operating results are also influenced by currency exchange rates between the Canadian dollar, U.S. dollar and British pound sterling. The Company has mitigated some of this risk by diversifying its borrowings to include U.S. and Canadian dollar debt.

Additional information may be found on the SEDAR website at www.sedar.com

# Management's Report

The accompanying consolidated financial statements of Bow Valley Energy Ltd. and all other financial and operating information contained in this Report are the responsibility of management. The consolidated financial statements have been prepared in accordance with accounting policies detailed in the notes to the consolidated financial statements and in accordance with generally accepted accounting principles in Canada.

The Company's systems of internal control have been designed and maintained to provide reasonable assurance that assets are properly safeguarded and that the financial records are sufficiently well maintained to provide relevant, timely and reliable information to management.

External auditors, appointed by the shareholders, have independently examined the consolidated financial statements. They have performed such tests as they deemed necessary to enable them to express an opinion on these consolidated financial statements.

An Audit Committee of the Board of Directors has reviewed these consolidated financial statements with management and the external auditors. The Board of Directors has approved the consolidated financial statements on the recommendation of the Audit Committee.

Robert G. Moffat
*President and Chief Executive Officer*

Matthew L. Janisch
*Vice President,*
*Finance and Chief Financial Officer*

March 5, 2007

**To the Shareholders of Bow Valley Energy Ltd.**

We have audited the consolidated balance sheets of Bow Valley Energy Ltd. as at December 31, 2006 and 2005 and the consolidated statements of operations and deficit and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2006 and 2005 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

PricewaterhouseCoopers LLP

*Chartered Accountants*
*Calgary, Alberta*

March 5, 2007

# Consolidated Balance Sheets

| As at December 31 | 2006 | 2005 |
|---|---|---|
| **ASSETS** | | |
| **Current assets** | | |
| Cash and cash equivalents | **$ 18,201** | $ 3,568 |
| Accounts receivable | **9,706** | 13,720 |
| Other *(note 4)* | **944** | 800 |
| | **28,851** | 18,088 |
| Property, plant and equipment *(note 2)* | **188,457** | 103,483 |
| Goodwill *(note 3)* | **8,512** | 8,512 |
| Future income tax asset *(note 7)* | **16,540** | – |
| Other assets *(note 4)* | **736** | 263 |
| | **$ 243,096** | $ 130,346 |
| **LIABILITIES** | | |
| **Current liabilities** | | |
| Accounts payable | **$ 43,782** | $ 13,760 |
| Risk management *(note 12)* | **82** | 240 |
| Bank indebtedness *(note 5)* | **76,384** | 8,847 |
| | **120,248** | 22,847 |
| Asset retirement obligation *(note 6)* | **11,939** | 11,023 |
| Future income tax liability *(note 7)* | **4,423** | 4,891 |
| **SHAREHOLDERS' EQUITY** | | |
| Share capital *(note 9)* | **118,302** | 102,724 |
| Contributed surplus *(note 8)* | **3,341** | 1,498 |
| Deficit | **(15,157)** | (12,637) |
| | **106,486** | 91,585 |
| | **$ 243,096** | $ 130,346 |

Commitments *(note 13)*

Contingencies *(note 14)*

Approved by the Board,

Daryl K. Seaman
Director

Jack W. Peltier
Director

# Consolidated Statements of Operations and Deficit

| For the years ended December 31 | **2006** | 2005 |
|---|---|---|
| **Revenue** | | |
| Operating | **$ 46,512** | $ 62,940 |
| Interest and other | **286** | 989 |
| Royalties (net of royalty tax credit) | **(7,491)** | (9,978) |
| | **39,307** | 53,951 |
| **Expenses** | | |
| Operating | **8,823** | 14,777 |
| Transportation | **793** | 910 |
| General and administrative | **8,239** | 5,252 |
| Interest | **1,059** | 1,162 |
| Foreign exchange loss (gain) | **3,735** | (159) |
| Risk management – unrealized | **(14)** | 1,070 |
| Risk management – realized | **420** | 928 |
| Depletion, depreciation and amortization | **18,810** | 19,993 |
| Accretion | **852** | 652 |
| | **42,717** | 44,585 |
| Net income (loss) before tax | **(3,410)** | 9,366 |
| **Taxes** | | |
| Current *(note 7)* | **22** | 19 |
| Future income tax expense (recovery) *(note 7)* | **(912)** | 2,869 |
| | **(890)** | 2,888 |
| **Net income (loss) for the period** | **(2,520)** | 6,478 |
| **Deficit** | | |
| Beginning of the year | **(12,637)** | (19,115) |
| End of the year | **$ (15,157)** | $ (12,637) |
| **Earnings (loss) per share** *(note 10)* | | |
| Basic and diluted | $ (0.04) | $ 0.10 |

# Consolidated Statements of Cash Flows

| For the years ended December 31 | **2006** | 2005 |
|---|---|---|
| **Operating Activities** | | |
| Net income (loss) for the year | **$ (2,520)** | $ 6,478 |
| Non-cash items | | |
| Foreign exchange – unrealized | **2,303** | – |
| Risk management – unrealized | **(14)** | 1,070 |
| Depletion, depreciation and amortization | **18,810** | 19,993 |
| Accretion | **852** | 652 |
| Stock based compensation | **1,934** | 992 |
| Future income tax expense (recovery) | **(912)** | 2,869 |
| Abandonment costs | **(76)** | (937) |
| Funds flow from operations | **20,377** | 31,117 |
| Premiums paid – risk management contracts *(note 4)* | **(617)** | (1,191) |
| Net change in non-cash working capital | **36,649** | (11,771) |
| | **56,409** | 18,155 |
| **Investing Activities** | | |
| Acquisition of property, plant and equipment | **(121,469)** | (39,513) |
| Net change in non-cash working capital | **(4,779)** | 166 |
| | **(126,248)** | (39,347) |
| **Financing Activities** | | |
| Issue of class A common shares for | | |
| Private placement | **16,965** | 21,805 |
| Exercise of options | **939** | 1,217 |
| Share issue costs | **(969)** | (1,090) |
| Bank indebtedness | **67,537** | (1,181) |
| | **84,472** | 20,751 |
| **Increase (Decrease) in cash** | **14,633** | (441) |
| **Cash and cash equivalents, beginning of period** | **3,568** | 4,009 |
| **Cash and cash equivalents, end of period** | **$ 18,201** | $ 3,568 |

Cash flow supplemental information – cash paid

| | | |
|---|---|---|
| Capital taxes paid | **22** | – |
| Interest paid | **5,059** | 1,108 |

For the years ended December 31, 2006 and 2005

## 1. Significant Accounting Policies

The consolidated financial statements of Bow Valley Energy Ltd. (the "Company") have been prepared in accordance with Canadian Generally Accepted Accounting Principles (GAAP).

**Management Estimates and Measurement Uncertainty**

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions regarding certain assets, liabilities, revenues and expenses. Such estimates include those related to unsettled transactions and events as of the date of the financial statements. Others include estimates related to depletion, depreciation, amortization, accretion, asset retirement obligations, future taxes, goodwill and the ceiling test. Actual results may differ from estimated amounts.

**Significant accounting policies are summarized as follows:**

**(a) Principles of consolidation**

The consolidated financial statements include the accounts of the Company and all of its subsidiaries.

**(b) Property, plant and equipment**

The Company follows the full cost method of accounting, whereby all costs associated with the exploration for and development of oil and gas reserves are capitalized and accumulated in country-by-country cost centres. Such costs include land acquisition, geological and geophysical, carrying of non-producing properties, drilling productive and non-productive wells, and plant and equipment.

Gains or losses on sales of properties are recognized only when crediting the proceeds to capitalized costs would result in a change of 20 percent or more in the depletion rate.

Depletion and depreciation of properties and equipment is provided using the unit-of-production method based on the Company's share of proved oil and natural gas reserves before royalties, as determined by independent engineers for each country. Production and reserves of natural gas are converted to barrels of oil equivalent (boe) using an energy equivalent basis of six thousand cubic feet of natural gas to one barrel of oil equivalent (6 mcf = 1 boe). This ratio is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead. In determining its depletion base, the Company includes estimated future costs to be incurred in developing proved reserves as estimated by independent engineers and excludes the cost of unproved properties. The unproved properties are assessed periodically to consider whether impairment has occurred. If an unproved property is considered to be impaired, the amount associated with the impairment is added to costs subject to depletion. Certain costs relating to North Sea and Alaska properties from which there has not been commercial production are not subject to depletion until commercial production commences.

Other capital assets are depreciated on a declining balance basis with rates as follows:

| | |
|---|---|
| Furniture & fixtures | 20% |
| Leasehold improvements | 20% |
| Office equipment | 20% |
| Computer hardware | 30% |
| Computer software | 100% |

The Company applies a ceiling test as a test of impairment of its capitalized costs relating to its petroleum and natural gas properties. The cost centres are tested for recoverability by comparison to undiscounted estimated future net revenues (cash flows) from proved reserves using forecast prices, plus the unimpaired cost of unproved properties. When the carrying amount of a cost center is not recoverable, the cost center is written down to its estimated fair value.

**(c) Goodwill**

Goodwill, which represents the excess of purchase price over estimated fair value of net assets received is not amortized but is assessed at least annually for impairment. To assess impairment, the fair value of the reporting unit is estimated and compared to the book value of the reporting unit. If the fair value is less than the book value, the amount of the impairment is determined by deducting the fair value of the reporting unit's identifiable assets and liabilities from the fair value of the reporting unit to determine the implied fair value of goodwill and comparing that amount to the book value of the reporting unit's goodwill. Any excess of the book value of goodwill over the implied fair value of goodwill is the impaired amount.

**(d) Asset retirement obligation**

The Company recognizes the estimated fair value of an asset retirement obligation (ARO) in the period in which it is incurred when a reasonable estimate of the fair value can be made. The fair value of the estimated ARO is recorded as a liability with a corresponding increase in the carrying amount of the related asset. ARO obligations are initially measured at fair value and subsequently adjusted for the accretion of discount and any changes to the underlying cash flows. The capitalized amount is depleted on a unit-of-production basis as part of the associated full cost pool over the life of the proved reserves. The liability amount is increased each reporting period due to the passage of time and the amount of accretion is charged to earnings in the period. Revisions to the estimated timing of cash flows or to the original estimated undiscounted cost result in an increase or decrease to the ARO. Actual costs incurred are charged against the ARO to the extent of the recorded liability.

**(e) Income taxes**

The Company follows the liability method of accounting for income taxes. Under this method, income tax liabilities and assets are recognized for the estimated tax effects of the differences between the amounts reported in the financial statements and the respective tax basis, using enacted income tax rates. The effect of a change in income tax rates on future income tax liabilities and assets is recognized in income in the period the change occurs.

Estimated future tax benefits related to losses and unclaimed costs for tax purposes are recognized as assets and in income, once it appears more likely than not they will ultimately be realized.

**(f) Flow-through shares**

The deductions for income tax purposes related to exploration and development activities funded by Canadian flow-through share arrangements are renounced to investors in accordance with income tax legislation. The future tax liability and a decrease to share capital is recorded when the applicable tax documents are filed with the authorities.

**(g) Stock option plan**

Bow Valley has a stock-based compensation plan that allows employees, consultants, and directors to purchase common shares of the Company. Option exercise prices approximate the five day weighted average market price of common shares prior to the date options are issued. Options granted under the plan vest over three years and expire five years after the grant date.

Stock based compensation expense is determined based on the estimated fair value of options on the date of grant. The fair value of options granted is estimated using the Black-Scholes option pricing model. Factors used in this model include expected volatility, expected dividends, and risk-free interest rates.

The compensation expense is recognized in earnings over the vesting period, with a corresponding increase to contributed surplus.

Consideration paid upon the exercise of the stock options is recorded as an increase to share capital together with corresponding amounts previously recognized in contributed surplus. Forfeitures are accounted for as they occur, which result in a reduction of compensation expense.

No amount of stock based compensation expense has been capitalized.

**(h) Risk management**

From time to time, the Company enters into risk management contracts for crude oil and natural gas prices on a portion of its production designed to reduce exposure to fluctuations in commodity prices and not for speculative purposes. The contracts are entered into with commodities trading institutions and may include costless collars, put options or fixed price contracts. The Company has not designated any of its risk management activities as accounting hedges under Accounting Guideline 13 and accordingly has marked to market its risk management contracts.

**(i) Cash and cash equivalents**

Cash and cash equivalents include interest-bearing short-term investments with maturity of three months or less when purchased.

Cash flows arising from risk management activities are classified as operating activities in the Consolidated Statement of Cash Flows.

**(j) Joint ventures**

Substantially all of the Company's exploration and development activities relating to oil and gas activities are conducted jointly with others. The accounts reflect the Company's proportionate interest in such activities.

**(k) Foreign currency translation**

The Company uses the temporal method for translating its foreign currency accounts and integrated foreign subsidiaries to Canadian dollars. Under this method, all monetary asset and liability accounts are translated to Canadian dollars at the exchange rate in effect at the balance sheet date and non-monetary assets and liabilities are translated at the exchange rate in effect when the assets were acquired or obligations incurred.

Revenues and expenses are translated to Canadian dollars at the monthly average exchange rate. Provisions for depletion, depreciation, and asset retirement obligation are translated at the same rate as the related balance sheet items. Foreign exchange gains and losses are included in earnings.

**(l) Comparative amounts**

Certain comparative figures have been reclassified to conform with the current year presentation.

## 2. Property, Plant and Equipment

| **December 31, 2006 ($000's)** | **Cost** | **Accumulated Depletion and Depreciation** | **Net Book Value** |
|---|---|---|---|
| **Oil and gas properties** | | | |
| **U.K.** | **$ 172,163** | **$ 64,029** | **$ 108,134** |
| **Canada** | **136,952** | **58,646** | **78,306** |
| **Alaska** | **1,859** | **–** | **1,859** |
| | **310,975** | **122,675** | **188,300** |
| **Other** | **1,085** | **928** | **157** |
| | **$ 312,060** | **$ 123,603** | **$ 188,457** |

| December 31, 2005 ($000's) | Cost | Accumulated Depletion and Depreciation | Net Book Value |
|---|---|---|---|
| Oil and gas properties | | | |
| U.K. | $ 101,325 | $ 59,188 | $ 42,137 |
| Canada | 105,738 | 44,476 | 61,262 |
| Alaska | – | – | – |
| | 207,063 | 103,664 | 103,399 |
| Other | 931 | 847 | 84 |
| | $ 207,994 | $ 104,511 | $ 103,483 |

At December 31, 2006, the net book value of U.K. oil and gas properties was $108.1 million (2005 – $42.1 million) of which $100.0 million (2005 – $26.2 million) consisted of unproved properties which were not depleted. During 2006, the Company recognized a $17.5 million (2005 – nil) future income tax asset which reduced the cost base of U.K. plant, property and equipment. The future income tax asset recognized relates to the future benefit of eligible capital exploration expenditures in accordance with the Exploration Expenditures Supplement enacted in the U.K.

At December 31, 2006, the net book value of Canadian oil and gas properties was $78.3 million (2005 – $61.3 million) of which $14.0 million (2005 – $9.1 million) consisted of unproved properties which were not depleted.

During 2006, the Company capitalized $1.0 million (2005 – $1.0 million) of overhead relating to exploration activities. The Company capitalized $6.8 million of interest in 2006 (2005 – nil). Depletion and depreciation amounted to $18.7 million (2005 – $19.6 million).

Bow Valley performed a ceiling test calculation at December 31, 2006, to assess the recoverable amount of the property, plant and equipment of the U.K. cost centre. The ceiling test indicated no impairment of the U.K. cost centre. The price forecast at December 31, 2006, used in this evaluation was the independent reserve evaluator's as outlined in the table below and adjusted for quality and transportation differentials specific to Bow Valley.

| Year | Exchange Rate C$/US$ | Brent US$/bbl | Natural Gas Price C$/mmbtu |
|---|---|---|---|
| 2007 | 0.87 | $ 60.50 | $ 8.81 |
| 2008 | 0.87 | $ 58.50 | $ 8.52 |
| 2009 | 0.87 | $ 56.50 | $ 8.23 |
| 2010 | 0.87 | $ 55.50 | $ 8.08 |
| 2011 | 0.87 | $ 55.50 | $ 8.08 |
| 2012 – 2017 | 0.87 | variable | variable |
| thereafter | 0.87 | +2%/year | +2%/year |

Bow Valley performed a ceiling test calculation at December 31, 2006, to assess the recoverable amount of the property, plant and equipment of the Canadian cost centre. The ceiling test indicated no impairment of the Canadian cost centre. The price forecast at December 31, 2006, used in this evaluation was the independent reserve evaluator's as outlined in the table below and adjusted for quality and transportation differentials specific to Bow Valley.

| Year | Exchange Rate C$/US$ | WTI US$/bbl | Edmonton Light C$/bbl | AECO C$/mmbtu |
|---|---|---|---|---|
| 2007 | 0.87 | $ 62.00 | $ 70.25 | $ 7.20 |
| 2008 | 0.87 | $ 60.00 | $ 68.00 | $ 7.45 |
| 2009 | 0.87 | $ 58.00 | $ 65.75 | $ 7.75 |
| 2010 | 0.87 | $ 57.00 | $ 64.50 | $ 7.80 |
| 2011 | 0.87 | $ 57.00 | $ 64.50 | $ 7.85 |
| 2012 – 2017 | 0.87 | variable | variable | variable |
| thereafter | 0.87 | +2%/year | +2%/year | +2%/year |

Future events, such as deteriorating operating performance or a reduction in commodity prices could result in material changes to the carrying amounts recognized in the Consolidated Financial Statements.

### 3. Goodwill

The Company tests Goodwill for impairment on at least an annual basis. At December 31, 2006, the estimated fair value of the Canadian reporting unit exceeded the carrying value of the unit including goodwill, indicating no impairment.

### 4. Other Assets

Current other assets include $0.8 million (2005 – $0.5 million) of oil produced but not sold at December 31, 2006, relating to U.K. operations. A cost recovery amount of $0.1 million (2005 – $0.3 million) in respect of the Company's service contract with the National Iranian Oil Company to develop the Balal oilfield has also been included in current other assets.

Non-current other assets include premiums of $0.7 million (2005 – $0.3 million) relating to U.K. put option contracts associated with the Company's risk management program.

### 5. Bank Indebtedness

In the U.K., the Company has bank facilities with approved limits totaling US$150.0 million, bearing interest at an interest rate ranging from LIBOR plus 1.5 percent for the senior facility and LIBOR plus 8.0 percent for the mezzanine facility. The approved limits are subject to semi-annual review and the facilities both expire on December 31, 2010. At December 31, 2006, US$43.7 million (2005 – US$3.0 million) was drawn on the facilities. The bank facilities are secured by a floating charge on all property, assets and rights of Bow Valley Petroleum (UK) Limited, and a guarantee from Bow Valley Energy Ltd.

In Canada, the Company had a $27.5 million revolving credit facility. At December 31, 2006, $25.5 million (2005 – $5.4 million) was drawn on this facility. The facility is repayable on demand, bears interest at the bank's prime rate plus 0.50 percent per annum, and is secured by a $50.0 million demand debenture conveying a fixed and floating charge over all properties in Canada. This facility is subject to semi-annual review each year. Subsequent to year-end, this facility was increased to $30.0 million, refer to Note 15, Subsequent Events.

### 6. Asset Retirement Obligation

The following table reconciles the asset retirement obligation associated with the retirement of oil and gas properties.

| ($000's) | 2006 | 2005 |
|---|---|---|
| Balance – beginning of the year | **$ 11,023** | $ 9,563 |
| Increase in obligations in the year | **138** | 113 |
| Settlement of obligations in the year | **(76)** | (937) |
| Revisions to estimates | **2** | 1,632 |
| Accretion expense | **852** | 652 |
| Balance – end of the year | **$ 11,939** | $ 11,023 |

The total future asset retirement obligation was estimated by management based on the Company's net ownership interest in wells and facilities, estimated costs to abandon the wells and facilities, reclamation of the land, and the estimated timing of the costs to be incurred in future periods. In Canada, the costs were estimated using the Energy Utilities Board guidelines for certain well and facility types and geographic areas. In the U.K., the costs were estimated by the Company's independent engineers. At December 31, 2006, the estimated net present value of the asset retirement obligation was $11.9 million ($7.7 million for the Company's U.K. operations and $4.2 million for the Canadian operations). The Company expects the undiscounted obligations of $18.9 million to become payable over the next 35 years with the majority between 2012 and 2019. A discount rate of between 6.5 and 7.4 percent and an inflation rate of 2.0 percent were used to calculate the present value of the asset retirement obligation.

## 7. Future Income Taxes

### Current Tax

The provision for income tax in the consolidated statement of operations and deficit varies from the amount that would be computed by applying the expected tax rate to earnings before income taxes. The principal reasons for differences between such "expected" income tax expense and the amount actually recorded are as follows:

| 2006 ($000's) | Canada | U.K. | Total |
|---|---|---|---|
| **Tax rate** | **34.50%** | **50.00%** | |
| **Expected income tax expense (recovery)** | **$ (1,677)** | **$ 1,552** | **$ (125)** |
| **Increase (decrease) in income taxes resulting from:** | | | |
| **Federal resource allowance** | **(510)** | **–** | **(510)** |
| **Non-deductible Crown charges** | **722** | **–** | **722** |
| **Alberta Royalty Tax Credit** | **(60)** | **–** | **(60)** |
| **Change in rates** | **(812)** | **–** | **(812)** |
| **Foreign exchange adjustment** | **–** | **(607)** | **(607)** |
| **Attributed Canadian Royalty Income** | **(184)** | **–** | **(184)** |
| **Non-deductible – other** | **706** | **–** | **706** |
| **Other** | **(42)** | **–** | **(42)** |
| **Actual income tax expense (recovery)** | **$ (1,857)** | **$ 945** | **$ (912)** |

| 2005 ($000's) | Canada | U.K. | Total |
|---|---|---|---|
| Tax rate | 37.62% | 50.00% | |
| Expected income tax expense (recovery) | $ 2,597 | $ 1,336 | $ 3,933 |
| Increase (decrease) in income taxes resulting from: | | | |
| Federal resource allowance | (1,572) | – | (1,572) |
| Non-deductible Crown charges | 1,969 | – | 1,969 |
| Alberta Royalty Tax Credit | (155) | – | (155) |
| Change in rates | (274) | 971 | 697 |
| Foreign exchange adjustment | – | 2,032 | 2,032 |
| Change in valuation allowance | – | (3,884) | (3,884) |
| Attributed Canadian Royalty Income | (111) | – | (111) |
| Non-deductible – other | 427 | | 427 |
| Other | (70) | (397) | (467) |
| Actual income tax expense (recovery) | $ 2,811 | $ 58 | $ 2,869 |

**Future Tax**

The figures in the tables below represent the differences between the accounting and tax basis of assets and liabilities at the tax rates expected to apply upon reversal of the differences.

| December 31, ($000's) | **2006** | 2005 |
|---|---|---|
| *Canada* | | |
| Net book value of property, plant and equipment in excess of tax basis | **$ (7,858)** | $ (8,978) |
| Asset retirement obligation | **1,228** | 1,217 |
| Non-capital loss carryforward | **1,256** | 1,910 |
| Share issue costs | **461** | 409 |
| Attributed Canadian royalty income | **490** | 609 |
| Future tax asset (liability) | **$ (4,423)** | $ (4,833) |
| *U.K.* | | |
| Net book value of property, plant and equipment in excess of tax basis | **$ (53,700)** | $ (17,318) |
| Asset retirement obligation | **3,890** | 3,700 |
| Loss carryforward | **61,216** | 13,560 |
| Exploration Expenditures Supplement | **5,134** | – |
| Future tax asset (liability) | **$ 16,540** | $ (58) |

**Tax Pools**

The approximate amounts of tax pools available are as follows:

| ($000's) | **2006** | 2005 |
|---|---|---|
| Canada | **$ 63,348** | $ 47,086 |
| United Kingdom | **127,750** | 34,329 |
| Total | **$ 191,098** | $ 81,415 |

**Tax Losses**

*Canada*

At December 31, 2006, the Company had losses (included in tax pools table above) available to offset future income for tax purposes of $4.1 million (2005 – $5.4 million). The losses expire in the years as noted:

| ($000's) | |
|---|---|
| 2007 | $ 1,315 |
| 2008 | 1,440 |
| 2009 | 1,315 |
| Total | $ 4,070 |

*U.K.*

At December 31, 2006, the Company had losses (included in tax pools table above) available to offset future income for tax purposes of $122.4 million (2005 – $27.1 million). The losses have an indefinite life.

## 8. Stock-Based Compensation

For 2006, $1.9 million (2005 – $1.0 million) was included in general and administrative expenses and credited to contributed surplus in respect of stock based compensation. The stock based compensation expense for option grants in the year are determined using the Black-Scholes option pricing model. The fair value of options granted in 2006 were calculated using a weighted average risk-free interest rate of 4.21%, an expected life of four years, a weighted average volatility of 45.38%, and no dividends. The weighted average fair value of options granted in 2006 was $2.28 per option.

| ($000's) | Contributed Surplus |
|---|---|
| As at December 31, 2004 | $ 521 |
| Stock based compensation | 992 |
| Transfer to share capital | (15) |
| As at December 31, 2005 | $ 1,498 |
| Stock based compensation | 1,934 |
| Transfer to share capital | (91) |
| **As at December 31, 2006** | **$ 3,341** |

## 9. Share Capital

### a) Authorized

Unlimited number of Class A, Class B and Class C Common Shares without nominal or par value.

Unlimited number of Class D, Class E and Class F Preferred Shares.

### b) Issued

| Class A Common Shares | Number | Amount ($000's) |
|---|---|---|
| As at December 31, 2004 | 64,641,547 | $ 80,367 |
| Options exercised | 883,634 | 1,217 |
| Transfer from contributed surplus | – | 15 |
| Private placement | 3,700,000 | 21,805 |
| Share issue costs | – | (1,090) |
| Tax effect of flow-through shares and issue costs | – | 410 |
| As at December 31, 2005 | 69,225,181 | $ 102,724 |
| Options exercised | 647,103 | 939 |
| Transfer from contributed surplus | – | 91 |
| Private placement | 2,900,000 | 16,965 |
| Share issue costs | – | (969) |
| Tax effect of flow-through shares and issue costs | – | (1,448) |
| **As at December 31, 2006** | **72,772,284** | **$ 118,302** |

### c) Stock Options

**Stock Option Reconciliation**

| Stock Option | Number of Options | Exercise Price | Weighted Average Exercise Price |
|---|---|---|---|
| Outstanding at December 31, 2004 | 4,305,033 | $0.50 – $2.41 | $1.53 |
| Granted | 1,617,367 | $1.89 – $4.61 | $3.35 |
| Exercised | (883,634) | $0.50 – $1.50 | $1.38 |
| Cancelled | (5,000) | $1.70 | $1.70 |
| Outstanding at December 31, 2005 | 5,033,766 | $0.95 – $4.61 | $2.15 |
| Granted | 1,067,500 | $5.07 – $6.51 | $5.64 |
| Exercised | (647,103) | $0.95 – $2.00 | $1.45 |
| Cancelled | – | – | – |
| **Outstanding at December 31, 2006** | **5,454,163** | **$1.31 – $6.51** | **$2.91** |

### Options Outstanding

| Range of Exercise Price | Number of Outstanding Options | Weighted Average Exercise Price | Weighted Average Remaining Contractual Life (Years) |
|---|---|---|---|
| $1.01 – $2.00 | 2,774,296 | $1.60 | 1.97 |
| $2.01 – $3.00 | 235,000 | $2.16 | 2.78 |
| $3.01 – $4.00 | 1,357,367 | $3.56 | 3.53 |
| $4.01 – $5.00 | 20,000 | $4.61 | 3.90 |
| $5.01 – $6.00 | 992,500 | $5.57 | 4.29 |
| $6.01 – $7.00 | 75,000 | $6.51 | 4.95 |
| Total | 5,454,163 | $2.91 | 2.86 |

### Exercisable Options

| Range of Exercise Price | Actual Number Outstanding | Weighted Average Exercise Price |
|---|---|---|
| $1.01 – $2.00 | 2,272,768 | $1.59 |
| $2.01 – $3.00 | 108,327 | $2.23 |
| $3.01 – $4.00 | 452,410 | $3.56 |
| $4.01 – $5.00 | 6,666 | $4.61 |
| Total | 2,840,171 | $1.94 |

## 10. Per Share Information

a) Basic per share information is calculated on the basis of the weighted average common shares outstanding during the year of 69,699,536 (2005 – 65,692,697).

b) Diluted per share information is calculated as the sum of the weighted average common shares outstanding during the period plus additional common shares to account for the dilutive effects of the Company's outstanding stock options during the period. The dilutive effect of outstanding options is calculated using the treasury stock method. The diluted weighted average number of common shares outstanding during the year was 72,278,143 (2005 – 67,589,100). This amount represents the sum of the weighted average common shares outstanding plus 2,578,607 (2005 – 1,896,403) common shares.

## 11. Geographic Segment Information

### Income

| 2006 ($000's) | Canada | U.K. | Other | Consolidated |
|---|---|---|---|---|
| Operating revenue | $ 30,534 | $ 15,978 | $ – | $ 46,512 |
| Interest and other income | – | 106 | 180 | 286 |
| Royalties, net of royalty tax credit | (7,189) | (302) | – | (7,491) |
| Operating expenses | (7,073) | (1,750) | – | (8,823) |
| Transportation expenses | (616) | (177) | – | (793) |
| General and administrative expense | (5,005) | (1,490) | (1,744) | (8,239) |
| Interest expense | (1,028) | (31) | – | (1,059) |
| Foreign exchange gain (loss) – realized | – | (1,532) | 100 | (1,432) |
| Foreign exchange gain (loss) – unrealized | – | (2,244) | (59) | (2,303) |
| Risk management gain – unrealized | – | 14 | – | 14 |
| Risk management loss – realized | – | (420) | – | (420) |
| Depletion, depreciation and amortization | (14,251) | (4,428) | (131) | (18,810) |
| Accretion expense of ARO | (232) | (620) | – | (852) |
| Taxes – current | (22) | – | – | (22) |
| – future income tax recovery (expense) | 1,857 | (945) | – | 912 |
| Net income (loss) for the period | $ (3,025) | $ 2,159 | $ (1,654) | $ (2,520) |

| 2005 ($000's) | Canada | U.K. | Other | Consolidated |
|---|---|---|---|---|
| Operating revenue | $ 40,474 | $ 22,466 | $ – | $ 62,940 |
| Interest and other income | 2 | 115 | 872 | 989 |
| Royalties, net of royalty tax credit | (9,335) | (643) | – | (9,978) |
| Operating expenses | (5,494) | (9,283) | – | (14,777) |
| Transportation expenses | (910) | – | – | (910) |
| General and administrative expense | (3,561) | (957) | (734) | (5,252) |
| Interest expense | (842) | (320) | – | (1,162) |
| Foreign exchange gain (loss) | – | 161 | (2) | 159 |
| Risk management loss – unrealized | – | (928) | – | (928) |
| Risk management loss – realized | – | (1,070) | – | (1,070) |
| Depletion, depreciation and amortization | (13,190) | (6,458) | (344) | (19,993) |
| Accretion expense of ARO | (240) | (412) | – | (652) |
| Taxes – current | (19) | | – | (19) |
| – future income tax expense | (2,811) | (58) | – | (2,869) |
| Net income (loss) for the period | $ 4,074 | $ 2,613 | $ (208) | $ 6,478 |

### Capital

| 2006 ($000's) | Canada | U.K. | Alaska | Other | Consolidated |
|---|---|---|---|---|---|
| Goodwill | $ 8,512 | $ – | $ – | $ – | $ 8,512 |
| Identifiable assets | $ 110,923 | $ 129,178 | $ 1,859 | $ 1,136 | $ 243,096 |
| Capital spending | $ 30,821 | $ 88,789 | $ 1,859 | $ – | $ 121,469 |

| 2005 ($000's) | | | | | |
|---|---|---|---|---|---|
| Goodwill | $ 8,512 | $ – | $ – | $ – | $ 8,512 |
| Identifiable assets | $ 79,934 | $ 48,917 | $ – | $ 1,495 | $ 130,346 |
| Capital spending | $ 28,025 | $ 11,488 | $ – | $ – | $ 39,513 |

## 12. Risk Management and Financial Instruments

During 2006, the Company incurred an unrealized gain of $0.01 million (2005 – loss of $1.1 million) and a realized loss of $0.4 million (2005 – realized loss of $0.9 million) due to the Company's risk management contracts.

As at December 31, 2006, the following risk management contracts were outstanding:

| | Time Frame | Basis | Volume (bbls) | Price (US$) |
|---|---|---|---|---|
| Costless Collars | | | | |
| Oil | First Half 2007 | Brent | 181,000 (floor) | 40.00 |
| | | | 90,500 (ceiling) | 67.50 |
| Puts | | | | |
| Oil | First Half 2007 | Brent | 181,000 | 40.00 |
| Oil | Third Quarter 2007 | Brent | 184,000 | 40.00 |
| Oil | Fourth Quarter 2007 | Brent | 228,160 | 40.00 |
| Oil | 2008 | Brent | 366,000 | 50.00 |

The Company's financial instruments are comprised of cash, accounts receivable, bank indebtedness, accounts payable and crude oil put and call options. The crude oil put and call options are marked to market on a quarterly basis. There are no significant differences between the carrying values of the other items and the estimated market values due to their short-term nature.

The Company is exposed to credit risk on its accounts receivable from its customers. The Company believes there is no significant concentration of credit risk.

The Company is exposed to interest rate risk to the extent of the floating rate related to bank indebtedness.

## 13. Commitments

As at December 31, 2006, the Company is committed in respect of office space and gathering and transportation contracts with payments as follows:

| ($000's) | Commitments |
| --- | --- |
| 2007 | $ 722 |
| 2008 | 73 |
| thereafter | – |
| Total | $ 795 |

The Company also had the following risk management obligations outstanding as at December 31, 2006:

| | Time Frame | Basis | Volume (bbls) | Price |
| --- | --- | --- | --- | --- |
| Call | First Half 2007 | Brent | 90,500 | US$67.50 |

The Company is participating in four field developments in the U.K. The Company will incur an estimated $65 million in capital costs over the next two years in respect of these developments. The timing and costs are subject to change based on the ability of the operators to complete the field developments as planned. The Company expects to finance these commitments through bank lines and funds flow from operations.

The Company entered into a joint venture agreement with Alaska Venture Capital Group, LLC in the fourth quarter of 2006. The Company has committed to spend an estimated $13 million in capital costs in 2007. The Company expects to finance these commitments through the recently completed $17 million equity financing which closed on December 11, 2006.

The Company has contracted a drilling rig for one North Sea offshore well expected to be drilled in the fourth quarter of 2007. The estimated financial commitment is approximately US$16.5 million.

## 14. Contingency

The Company is currently engaged in legal proceedings to defend an action regarding its interest in the Balal (Iran) project. It is the Company's opinion that the action is frivolous and without merit. Potential damages are not quantifiable at this time, but in any event, are not likely to be material to the Company. During 2006, $1.7 million (2005 – $0.7 million) was included in general and administrative costs in respect of legal defense costs.

## 15. Subsequent Events

On February 20, 2007, the Company announced that it had engaged a financial advisor to assist in evaluating strategic alternatives for its Canadian subsidiary. While it is likely that this process will lead to the disposition of all or a portion of the Canadian assets, there is no assurance that this will be the case, nor is any forecast given as to the form of action that will be taken, if any. An estimate of the financial impact, if any, of the potential disposition cannot be made at the current time.

On February 21, 2007, the Company agreed to a new bank line with the National Bank of Canada regarding its Canadian assets. The new line consists of a $22.5 million senior facility plus a $7.5 million term facility due May 31, 2007. The Company believes this new facility will be adequate to meet its near term capital and liquidity needs. The term facility is expected to be repaid through cash flow and the sale of some or all of the Canadian assets.

The Board and management recognize that effective corporate governance is important to the direction and operation of the Company. As a result, Bow Valley has developed and implemented, and continues to develop, implement and refine formal policies and procedures which reflect our ongoing commitment to good corporate governance and which encourage a culture of integrity, honesty and respect.

## COMPOSITION OF THE BOARD

The Board of Directors consisted of six individuals in 2006, including a non-executive Chairman of the Board and the President and Chief Executive Officer of the Company. Five of the six directors, including the Chairman of the Board, are considered independent within the meaning of applicable securities legislation.

The Board has responsibility for appointing senior management and supervising and overseeing the management of the Company. In addition to the obligations of the Board mandated by law, the Board has responsibility for strategic planning, the selection and monitoring of management and the identification of the principal risks associated with Bow Valley's business. These duties and responsibilities, among others, are set forth in a written mandate that has been adopted by the Board. The Board of Directors mandate is attached as Schedule B of the Information Circular. The Board approves all significant decisions that materially affect the Company before they are implemented and annually approves the Company's key business and financial objectives.

Certain powers, duties and responsibilities of the Board have been delegated to committees of the Board, as described below.

## COMMITTEES

During the year ended December 31, 2006, the Board of Directors had five committees – the Audit Committee, the Reserves Committee, the Compensation and Corporate Governance Committee, the Hedging Committee and the Nominating Committee. The Company also has a Management Disclosure Committee comprised of members of management, including the President and CEO, and all Vice-Presidents. Committee Membership in each committee is set forth below. For information on the attendance of members at each of the committee meetings, see "Annual Meeting Business – Election of Directors – Meetings Held and Attendance of Directors" in the Information Circular available on SEDAR at www.sedar.com.

### Audit Committee

The Audit Committee is comprised of Messrs. Jack W. Peltier (Chairman) Henry R. Lawrie, Gerald J. Maier and George Y. Tooley. All members are directors who are considered independent within the meaning of applicable securities legislation.

The Audit Committee is responsible for assisting the Board of Directors in fulfilling its oversight responsibilities in respect of the review and approval of the financial statements and reporting processes of the Company, review of the system of internal controls that management has established and for overseeing the external audit process. The Audit Committee has a direct communication channel with the external auditors and meets with them independently of management.

**Reserves Committee**

The Reserves Committee is comprised of Messrs. Henry R. Lawrie (Chairman), Gerald J. Maier and Jack W. Peltier. All members are directors who are considered independent within the meaning of applicable securities legislation.

The Reserves Committee is responsible for assisting the Board of Directors in fulfilling its oversight responsibilities in respect of the reserves evaluation process. The Reserves Committee meets with the independent engineers to assess the methodology used in estimating the reserves and to consider whether adequate information is made available for their assessment and that management co-operates in making such information available. The Reserves Committee has a direct communication channel with the independent engineers and meets with them independently of management.

**Compensation and Corporate Governance Committee**

The Compensation and Corporate Governance Committee is comprised of Messrs. Henry R. Lawrie (Chairman), Daryl K. Seaman and George Y. Tooley, directors who are considered independent within the meaning of applicable securities legislation.

The Compensation and Corporate Governance Committee is responsible for assisting the Board of Directors in fulfilling its corporate governance role and approving the overall compensation policies of the Company. The committee also has the responsibility of monitoring and considering the effectiveness of the Board, its committees and the individual directors, including the composition and size of the Board and its committees and the compensation of the Board members.

**Nominating Committee**

The Nominating Committee is comprised of Messrs. Daryl K. Seaman (Chairman), Henry R. Lawrie and Jack W. Peltier, directors who are considered independent within the meaning of applicable securities legislation.

The Nominating Committee is responsible for assisting the Board of Directors in fulfilling its oversight responsibilities in respect of determining the competencies and skills that the Board of Directors, as a whole, should possess. The Nominating Committee also has the responsibility for recommending new candidates for election to the Board of Directors and for the orientation of new directors.

**Hedging Committee**

The Hedging Committee is comprised of Messrs. Robert G. Moffat (Chairman), Gerald J. Maier and George Y. Tooley. Messrs. Maier and Tooley are directors who are considered independent within the meaning of applicable securities legislation, whereas Mr. Moffat is a member of management.

The Hedging Committee is responsible for assessment and review of the Company's risk management activities.

### Disclosure Committee

The Disclosure Committee is comprised of Messrs. Robert G. Moffat (Chairman), Matthew L. Janisch, Thomas J. Ruissen, John W. Essex and David A. Fleming, all of whom are members of management.

The Disclosure Committee is responsible for oversight of the Company's disclosure controls and procedures and endevouring to ensure the Company meets all regulatory disclosure requirements. The Disclosure Committee reviews and, as necessary, helps revise the Company's disclosure controls and other procedures in a manner designed to ensure that information required to be disclosed by securities regulators and the Toronto Stock Exchange, and other information the Company discloses to the public is recorded, processed, summarized and reported accurately and on a timely basis.

## CORPORATE POLICIES

### Corporate Disclosure Policy

The Disclosure Policy confirms in writing the existing disclosure policies and practices of the Company. The goal of the policy is to promote appropriate and consistent disclosure practices aimed at accurate, informative, timely and broadly disseminated disclosure of material information to the market and to promote compliance among the directors, officers, employees and consultants of the Company.

The policy covers written disclosure in documents filed with the securities commissions and stock exchanges, written statements made in the Company's annual and quarterly reports, news releases, letters to shareholders and other documents released to the public, the content of which would reasonably be expected to affect the market price or value of the Company's securities, or a reasonable investor's investment decision, including information contained on the Company's website and other electronic communications. The policy also extends to public oral statements made in meetings and telephone conversations with analysts and investors, interviews with the media, press conferences, conference calls and in other circumstances in which it is reasonable to expect that the information will become generally disclosed.

### Code of Business Conduct

The Code of Business Conduct applies to all directors, officers, employees and consultants of the Company. The Board of Directors is responsible for monitoring compliance with the Code of Business Conduct and for approving any waivers of such standards by any director or officer. Waivers in respect of employees or consultants may be given by the President and Chief Executive Officer who must report any such waiver to the Board.

The Code of Business Conduct addresses such matters as conflicts of interest, confidential information, and the protection and proper use of the Company's assets. All directors, officers, employees and consultants are encouraged to report violations of the Code of Business Conduct in accordance with the procedures described in the Company's whistleblower policy.

### Whistleblower Policy

The purpose of the Whistleblower Policy is to maintain a workplace where concerns regarding questionable practices can be raised without fear of any discrimination, retaliation or harassment. The Whistleblower Policy encourages all directors, officers, employees and consultants to promptly report either orally or in writing any activity that may constitute questionable accounting or auditing practices; inadequate internal accounting controls; misleading or coercion of auditors; disclosure of fraudulent or misleading financial information; instances of corporate fraud; a material misrepresentation in any written or oral disclosure made by or on behalf of the Company; breaches of the Company's policy on trading in securities; and other activities which may violate the Company's Code of Business Conduct.

The Whistleblower Policy outlines several means by which concerns may be reported, including communication with an immediate supervisor, an officer or director of the Company, or contact with the Chairman of the Audit Committee. Contact by mail, telephone, fax or email is encouraged. All reports made to supervisors and officers in respect of matters specifically covered by the Whistleblower Policy are to be reported to the Audit Committee of the Board of Directors.

### Policy on Trading in Securities by Directors, Officers, Employees and Consultants

The purpose of the Policy on Trading in Securities by Directors, Officers, Employees and Consultants is to ensure compliance with provincial securities laws governing trading while in possession of material non-public information concerning the Company. The Policy also prohibits tipping or disclosing material non-public information to outsiders.

The scope of the Policy is defined to include family and household members; shares directly or indirectly owned; and shares over which control or direction is exercised. The Policy defines 'material non-public information', outlines prohibited activities, and provides information regarding blackout periods and reporting requirements for insiders. The Policy outlines some of the penalties of prohibited trading and/or tipping under securities laws, as well as the potential disciplinary actions by the Company.

**Daryl K. Seaman, O.C.**
*Chairman of the Board*
Mr. Seaman is Chairman of the Board and a founder of Bow Valley Energy Ltd. From 1992 to present, he has been Chairman and President of Dox Investments Inc., a private holding company. From 1949 through 1992, he was Chairman, Chief Executive Officer and Director of Bow Valley Industries Ltd. and its predecessor companies which he co-founded. Mr. Seaman is also a director of Far West Mining Ltd. and Pure Technologies Ltd. Mr. Seaman is an Officer of the Order of Canada.

**Robert G. Moffat**
*President, Chief Executive Officer and Director*
Mr. Moffat graduated from Queen's University in Kingston, Ontario in 1977 with a B.Sc. (Geology) degree. From 1995 to 2001, he was President, Chief Executive Officer and Director of Courage Energy Inc. From 1992 though 1995, he was President of Springsyde Resources Ltd., a company he founded and which later became Courage Energy Inc. through an amalgamation and name change in 1995. Prior thereto, he was Vice President and Director of Highridge Exploration Ltd. Mr. Moffat has been instrumental in directing corporate growth through oil and natural gas exploration in Canada, the United States and internationally. Mr. Moffat is also a director of Global Energy Services Ltd. and Sylogist Ltd.

**Henry R. Lawrie**
*Director*
Mr. Lawrie joined Price Waterhouse in Calgary, was admitted to partnership in 1971 and served as a partner in Calgary, Toronto, Dallas and Midland, Texas. He was Co-Chairman, Price Waterhouse Canada Oil and Gas Specialty; Managing Partner, Price Waterhouse, Calgary; and was twice elected to the Price Waterhouse Canada Policy Board. He retired from Price Waterhouse in June 1997. In addition, Mr. Lawrie was Chief Accountant of the Alberta Securities Commission from 1997 through 2001, Chair of the Oil and Gas Securities taskforce, and Advisor to the Commission. Mr. Lawrie is a director of several public companies including Berens Energy Ltd., Delphi Energy Corp., Flagship Energy Inc. and Storm Exploration Inc.

**Gerald J. Maier, O.C.**
*Director*
Mr. Maier has extensive experience in the energy industry, including roles as Chairman and CEO of Hudson's Bay Oil and Gas and TransCanada PipeLines and CEO of Bow Valley Industries. Mr. Maier is currently Chairman of Granmar Investments Ltd., a private investment company, and sits on the boards of Stream-Flo Industries Ltd., Master Flo Valves Inc., Gem Inc., and Willbros Group, Inc. He is a Fellow of the Canadian Academy of Engineering and was invested as an Officer to the Order of Canada in 2003 for his various roles focusing on social responsibility. Mr. Maier holds a B.Sc. degree in Petroleum Engineering from the University of Alberta.

**Jack W. Peltier**
*Director*
Mr. Peltier is currently President of Ipperwash Resources Ltd., a company engaged in oil and natural gas production, investments and consulting services. He is a director of Ember Resources Inc. and Masters Energy Inc., both public companies; a director of Tundra Oil & Gas Limited and Strand Resources Ltd., both private companies; and a member of the board of trustees of Paramount Energy Trust and Gienow Income Trust, both of which are publicly listed.

**George Y. Tooley**
*Director*
Mr. Tooley is currently a principal of the Petrovest Group. He has been actively involved in the financing and administration of petroleum and mining projects for the last 16 years. Mr. Tooley is President of a private holding company. From 1995 to 2005, he was Vice President and Director of Fairstar Explorations Inc., a public mining exploration company. From 1992 through 2001, he was a Director of Courage Energy Inc., a public oil and natural gas company.

**Robert G. Moffat**

*President, Chief Executive Officer and Director*

Mr. Moffat graduated from Queen's University in Kingston, Ontario in 1977 with a B.Sc. (Geology) degree. From 1995 to 2001, he was President, Chief Executive Officer and Director of Courage Energy Inc. From 1992 though 1995, he was President of Springsyde Resources Ltd., a company he founded and which later became Courage Energy Inc. through an amalgamation and name change in 1995. Prior thereto, he was Vice President and Director of Highridge Exploration Ltd. Mr. Moffat has been instrumental in directing corporate growth through oil and natural gas exploration in Canada, the United States and internationally. Mr. Moffat is also a director of Global Energy Services Ltd. and Sylogist Ltd.

**Matthew L. Janisch**

*Vice President, Finance and Chief Financial Officer*

Mr. Janisch, B.Sc., MBA, graduated with a Masters of Business Administration from the University of Western Ontario in 1991 and a B.Sc. (Petroleum Engineering) degree from the University of Alberta in 1984. He has over 20 years of experience in banking, corporate finance, capital markets and oil and natural gas research and engineering. Previously, Mr. Janisch was Managing Director of Oil and Natural Gas Equity Research at a major Canadian bank, where his responsibilities included equity coverage of senior domestic and international E&P companies as well as commodity price forecasting. He also has extensive experience in investment banking within the oil and natural gas sector, including debt and equity issues as well as mergers and acquisitions.

**John W. Essex**

*Vice President, Operations*

After graduating from the University of British Columbia with a B.A. Sc. (Geological Engineering) degree, Mr. Essex began his career as a reservoir engineer at Shell Canada in 1975. He has over 30 years of diversified oil and natural gas industry experience. For the past 20 years, he has held the senior production role at various Calgary-based oil and natural gas companies. In this capacity, Mr. Essex has had responsibility for the production, operations, safety/environment, engineering, marketing and property A&D functions and has successfully applied his expertise in the areas of asset optimization, reservoir management/analysis and property evaluation.

**Thomas J. Ruissen**

*Vice President, Exploration*

Mr. Ruissen has 23 years of oil and natural gas industry experience focused on the western Canadian Sedimentary Basin. Since his graduation in 1982 from the University of British Columbia with a B.Sc. (Geology) degree, Mr. Ruissen has held positions of increasing responsibility with Amoco Canada Petroleum Co. Ltd., Rigel Oil & Gas Ltd. and Baytex Energy Ltd. He has held management and senior management positions for the past nine years. In these positions, Mr. Ruissen has led exploration-oriented, multi-disciplinary units charged with providing economic growth of light oil and natural gas reserves and production. His responsibilities have included overseeing group performance, technical proficiency, operational efficiency and providing strategic direction. He has provided leadership, mentoring, direction and focus to the units while continuing to function as a prospect generator.

**David A. Fleming**

*Vice President, International*

Mr. Fleming joined Bow Valley in 1997 following 30 years in a number of engineering and management positions with the Shell group of companies in Canada, Australia and Oman. His experience covers research and development, natural gas marketing, project development and project management, latterly as Chief Executive and General Manager during the initial phase of development of a major LNG facility in Oman.

**Nick J. Fairbrother**

*Managing Director, Bow Valley Petroleum (UK) Limited*

Mr. Fairbrother has 29 years of diverse oil and natural gas experience in the North Sea. He has full responsibility for Bow Valley's U.K. operations. Since his graduation in 1977 from Birmingham University with a B.Sc. (Chemical Engineering) degree, Mr. Fairbrother has held technical and management positions of increasing responsibility with Amoco (UK) Exploration, Shell UK, Kerr-McGee and Amerada Hess. As Vice President, Production at Amerada Hess, Mr. Fairbrother was responsible for all operations in Europe, North Africa and Asia. In 2002, he co-chaired a joint industry group which introduced the United Kingdom's new Fallow Acreage rules.

| | **2006** | 2005 | 2004 | 2003 | 2002 |
|---|---|---|---|---|---|
| **FINANCIAL** | | | | | |
| ($000s except per share amounts) | | | | | |
| Revenue | **46,512** | 62,940 | 37,419 | 42,574 | 31,605 |
| Funds flow | **20,377** | 31,117 | 14,530 | 23,633 | 13,613 |
| Basic per share ($/share) | **0.29** | 0.47 | 0.23 | 0.38 | 0.27 |
| Diluted per share ($/share) | **0.28** | 0.46 | 0.23 | 0.38 | 0.27 |
| Earnings (loss) | **(2,520)** | 6,478 | (3,201) | 3,849 | 4,603 |
| Basic per share ($/share) | **(0.04)** | 0.10 | (0.05) | 0.06 | 0.09 |
| Diluted per share ($/share) | **(0.04)** | 0.10 | (0.05) | 0.06 | 0.09 |
| Capital expenditures | **121,469** | 39,513 | 28,873 | 27,983 | 51,021 |
| Total assets | **243,096** | 130,346 | 104,258 | 90,463 | 85,144 |
| Working capital (deficit) | **(91,397)** | (4,759) | (16,023) | (2,829) | (4,850) |
| Shares (000s) | | | | | |
| Basic outstanding at year-end | **72,772** | 69,225 | 64,642 | 64,510 | 61,844 |
| Outstanding options and warrants | **5,454** | 5,034 | 4,305 | 3,433 | 3,479 |
| Weighted average | **69,700** | 65,693 | 64,578 | 62,019 | 51,040 |

| | **2006** | 2005 | 2004 | 2003 | 2002 |
|---|---|---|---|---|---|
| **OPERATING** | | | | | |
| **Sales volumes** | | | | | |
| Crude oil and NGL (bbl/d) | | | | | |
| U.K. | **527** | 815 | 497 | 1,002 | 1,358 |
| Canada | **391** | 276 | 200 | 326 | 101 |
| Total | **918** | 1,091 | 697 | 1,328 | 1,459 |
| Natural gas (mmcf/d) | | | | | |
| U.K. | **0.7** | 2.3 | 3.3 | 3.9 | 2.0 |
| Canada | **8.4** | 10.5 | 8.3 | 7.2 | 3.7 |
| Total | **9.1** | 12.8 | 11.6 | 11.1 | 5.7 |
| Barrels of oil equivalent (boe/d) | | | | | |
| U.K. | **647** | 1,195 | 1,053 | 1,652 | 1,698 |
| Canada | **1,796** | 2,032 | 1,590 | 1,525 | 711 |
| Total | **2,443** | 3,227 | 2,643 | 3,177 | 2,409 |
| **Reserves** | | | | | |
| Crude oil and NGL (mbbls) | | | | | |
| Proved | | | | | |
| U.K. | **4,235** | 3,247 | 550 | 834 | 1,980 |
| Canada | **562** | 494 | 315 | 189 | 250 |
| Probable | | | | | |
| U.K. | **6,429** | 7,016 | 10,850 | 11,810 | 12,600 |
| Canada | **304** | 227 | 182 | 64 | 70 |
| Natural gas (bcf) | | | | | |
| Proved | | | | | |
| U.K. | **4.2** | 4.4 | 6.0 | 7.3 | 9.3 |
| Canada | **11.7** | 14.8 | 13.2 | 8.1 | 9.7 |
| Probable | | | | | |
| U.K. | **11.8** | 11.3 | 12.4 | 14.4 | 20.3 |
| Canada | **6.1** | 6.7 | 6.5 | 2.9 | 2.5 |
| **Undeveloped land** (net acres – 000s) | | | | | |
| U.K. | **50** | 79 | 42 | 41 | 104 |
| Canada | **64** | 60 | 51 | 45 | 38 |
| United States | **8** | – | – | – | – |
| France | **–** | – | – | – | 283 |
| Total | **122** | 139 | 93 | 86 | 425 |

**BOARD OF DIRECTORS**

**Daryl K. Seaman**, O.C. (1) (5)
*Chairman of the Board*
Calgary, Alberta

**Robert G. Moffat** (4)
*President, Chief Executive Officer and Director*
Calgary, Alberta

**Henry R. Lawrie** (1) (2) (3) (5)
*Director*
Calgary, Alberta

**Gerald J. Maier**, O.C. (2) (3) (4)
*Director*
Calgary, Alberta

**Jack W. Peltier** (2) (3) (5)
*Director*
Calgary, Alberta

**George Y. Tooley** (1) (2) (4)
*Director*
Calgary, Alberta

(1) Member of the Compensation and Corporate Governance Committee
(2) Member of the Audit Committee
(3) Member of the Reserves Committee
(4) Member of the Hedging Committee
(5) Member of the Nominating Committee

**MANAGEMENT**

**Robert G. Moffat**
*President, Chief Executive Officer and Director*

**John W. Essex**
*Vice President, Operations*

**David A. Fleming**
*Vice President, International*

**Matthew L. Janisch**
*Vice President,*
*Finance and Chief Financial Officer*

**Thomas J. Ruissen**
*Vice President, Exploration*

**Nick J. Fairbrother**
*Managing Director,*
*Bow Valley Petroleum (UK) Limited*

**CORPORATE SECRETARY**

**R.J. (Bob) Engbloom**

**CORPORATE OFFICE**

Bow Valley Energy Ltd.
1200, 333 Seventh Avenue SW
Calgary, Alberta, Canada T2P 2Z1
Telephone: (403) 232 0292
Facsimile: (403) 232 8920
E-mail: bve@bvenergy.com
Website: www.bvenergy.com

**UNITED KINGDOM OFFICE**

Bow Valley Petroleum (UK) Limited
2 Thames Avenue
Windsor, Berkshire, England SL4 1QP
Telephone: +44 (0) 1753 753 800
Facsimile: +44 (0) 1753 753 809

**BOARD OF DIRECTORS (U.K.)**

Christopher D. Longman
David A. Fleming
Robert G. Moffat
Walter R. Roberts
Matthew L. Janisch
Nick J. Fairbrother

**BOW VALLEY ALASKA OFFICE**

Bow Valley Alaska Corporation
1200, 333 Seventh Avenue SW
Calgary, Alberta, Canada T2P 2Z1
Telephone: (403) 232 0292
Facsimile: (403) 232 8920

**BOARD OF DIRECTORS (ALASKA)**

David B. Orser
Matthew L. Janisch

**AUDITORS**

PricewaterhouseCoopers LLP

**BANKERS**

Bank of Scotland
National Bank of Canada

**REGISTRAR AND TRANSFER AGENT**

Valiant Trust Company

**SOLICITORS**

Macleod Dixon LLP

**INDEPENDENT ENGINEERS**

GLJ Petroleum Consultants Ltd.

**STOCK EXCHANGE LISTING**

Toronto Stock Exchange
Trading Symbol: BVX

**ANNUAL INFORMATION FORM**

The Annual Information Form can be obtained on request from the Company, or from the Company's website, or from SEDAR at www. sedar.com.

**Forward-looking Information**

This document may contain forward-looking statements or forward-looking information under applicable securities legislation. Forward-looking statements or information typically contain statements with words such as "anticipate", "believe", "expect", "plan", "intend", "estimate", "propose", or similar words suggesting future outcomes or statements regarding an outlook. Although the Company believes that the expectations reflected in such forward-looking statements or information are reasonable, undue reliance should not be placed on forward-looking statements because the Company can give no assurance that such expectations will prove to be correct. Forward-looking statements or information are based on current expectations, estimates and projects that involve a number of risks and uncertainties which could cause actual results to differ materially from those anticipated by the Company and described in the forward-looking statements or information. The forward-looking statements or information contained in this document are made as of the date produced and the Company undertakes no obligation to update publicly or revise any forward-looking statement or information, whether as a result of new information, future events or otherwise, unless so required by applicable securities laws. The forward-looking statements or information contained in this document are expressly qualified by this cautionary statement.

Printed in Canada

Produced by Conduit Corporate Communications Inc.

# Bow Valley Energy Ltd.

1200, 333 Seventh Avenue SW
Calgary, Alberta, Canada T2P 2Z1
Telephone: (403) 232 0292
Facsimile: (403) 232 8920
Email: bve@bvenergy.com
Website: www.bvenergy.com
**TSX: BVX**